MPHIL

Transnational joint ventures and acquisitions in the mechanical engineering industry in the E.E.C.

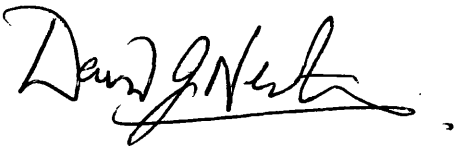
Newton, David J.

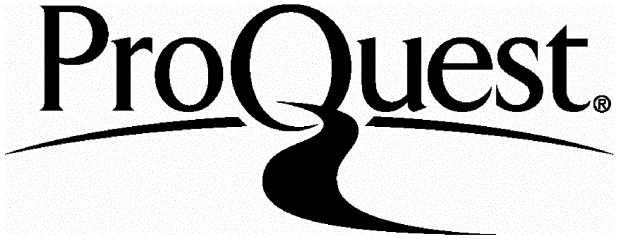
Award date:
1983

Awarding institution:
University of Bath

TRANSNATIONAL JOINT VENTURES AND ACQUISITIONS IN THE MECHANICAL ENGINEERING INDUSTRY IN THE E.E.C.

submitted by David J.Newton
for the degree of M.Phil.
of the University of Bath
1983.





SUMMARY

The main emphasis of this thesis has been the study of joint ventures, with acquisitions being analysed as an alternative and comparable strategy.

The Introduction seeks to answer the questions of how many transnational joint ventures and acquisitions have taken place within the EEC in recent years, and how they have been distributed on a regional and industrial basis.

Chapter One examines previous studies on joint ventures with respect to the structural effects of co-operation on the industry, notably upon competition.

This theme is developed in Chapter Two, which looks at joint ventures in the light of EEC competition policy. The attitudes of the EC Commission towards co-operation are examined, together with attempts by the Commission to enhance the prospects for transnational co-operation and to create a more uniform competitive environment across the EEC.

Chapter Three then examines the firm's point of view, and is thus concerned with the relevant aspects of corporate strategy. Different entry strategies for firms seeking to penetrate EEC markets are described, with an emphasis on joint ventures and acquisitions, together with some of the issues involved in planning, setting up and running such operations.

The thesis has concentrated on the mechanical engineering industry, background information on which is the basis of Chapter Four. This shows the importance of international trade, and thus highlights the relevance of transnational strategy, to this industry.

Chapter Five draws together themes from the earlier chapters and shows their influences on the central part of this thesis, a survey of engineering companies throughout the UK and EEC which have engaged in transnational joint ventures and acquisitions. This chapter also describes the methodology of the research programme.

The results of the survey are described in Chapters Six and Seven.

The study was financed by the Social Science Research Council, whose support is acknowledged.

-----oOo-----

C O N T E N T S

-----oOo-----

LIST OF TABLES

-----oOo-----

INTRODUCTION

This study is concerned with transnational business collaboration of all kinds in the Mechanical Engineering sector in the EEC, and with Joint Ventures in particular. The EC Commission defines a joint venture as follows : "A joint venture is generally defined as an enterprise subject to joint control by two or more undertakings which are economically independent of each other." [1]

However, joint ventures (JVs) represent only one of the strategies available to companies for expanding their business. In order to assess the significance of the results, the study has also examined other strategies, in particular takeovers. The principal effect of this is that a comparison and contrast of JVs and takeovers, which have been examined in approximately equal numbers by use of a questionnaire, has been made possible.

There are no comprehensive figures on the numbers of joint ventures, takeovers and share participations taking place in the EEC. The EC Commission does make some estimates, recorded in its annual Report onm Competition Policy. But although these statistics (discussed at greater length on pp. 3-9) appear at first sight to be comprehensive, this is not so. Members of the Competition Policy Directorate (DGIV) at the European Commission pick reports on joint ventures out of selected European newspapers. The Commission then checks that the firms concerned have applied to the EEC for exemption from Article 85(1) of the Treaty of Rome, contained in the Rules on Competition Policy, under the 'escape' clause contained in Article 85(3) (see appendix 2).

The collection of statistics is simply a by-product of this process and is not pursued as an end in itself.

In addition, the Commission's definition of a joint venture is confined to those cases in which a new joint company is created - the 'equity JV' - and excludes what shall later be described as 'the contractual JV'. Finally, of course, any venture which is not featured in those newspapers is not included in the JV statistics.

---

[1] EC Commission, Fourth Report on Competition Policy, Brussels & Luxembourg, April 1975.

In short, then, there is no record of the true number of joint operations taking place in the EEC.

The EC Commission has in recent years been concerned at the domination of many markets by North American, and now increasingly Japanese, multinational corporations. In 1973, for example, two large multinationals in the construction equipment sector spent as much on research and development as the entire UK mechanical engineering industry put together.[1] Because of the large number of firms, much of the European R & D would have represented duplication of effort.[2]

The Commission would like to see some rationalisation, particularly at the lower end of the scale. It would like firms which are small and medium-sized on a national scale combine on a European scale in order to compete more effectively with these very large corporations.

There is some concern at the Commission, however, that co-operation between large concerns would have rather different effects. The danger in encouraging co-operation is that large firms can enter price-fixing or market sharing agreements, which would contravene the EEC rules on Competition Policy.

Much of the literature on the subject of JVs (which is predominantly from the USA) has concentrated on this question, of whether JVs do in fact produce anti-competitive effects, though there is evidence that US JVs frequently occur as a response to the very strong anti-trust regulations which exist in the USA and which more or less prohibit mergers or takeovers of any significant size.

---

[1] NEDC Industrial Strategy Report, Construction Equipment and Mobile Cranes Sector Working Party, September 1976, p.8

[2] For evidence that JVs can eliminate duplicative R & D see pp. 36 and 208.

Much has also been written on JVs which are undertaken by (predominantly US) multinational corporations (MNCs) in underdeveloped countries. Generally, however, these ventures are forced on such companies by political considerations or, indeed, because local legislation stipulates that a foreign company cannot own more than a certain percentage of a local enterprise.

In the EEC, no such regulations exist, though there may well be political pressures. Subject to such pressures, and also to national competition regulatory bodies such as the Monopolies Commission and EEC competition law (Article 85 of the Treaty of Rome, relating to concerted practices, and Article 86, relating to exploitation of a dominant position), companies are free to set up by themselves in a 'greenfield' venture, take over other companies or set up joint ventures.

The EC Commission is unable to estimate the proportion of intra-EC trade done through JVs, although JVs are in most cases one possible strategy. But because of the lack of previous literature on intra-EC JVs, companies wishing to know more about this strategy can only learn from their own experience, which can be a very expensive way of learning.

The results of the present study show that JVs are generally very small in relation to the size of the parent companies.[1] US writers who suggest that JVs are anticompetitive would claim, however, that the importance of JVs extends beyond their mere size.[2]

- Share Purchases, Joint Ventures, Takeovers and Mergers in the Community, 1973-80.

i) Type of Operation.

The total number of operations recorded by the Commission (bearing in mind that the Commission has no record of the true total), comprising takeovers and mergers, share purchases and joint ventures taking place in the Community grew from 1,638 in 1973 to 2,419 in 1980 - an increase of almost 50% in the annual rate, although the 1980 figure represents a fall of 17% from the 1979 total (see Table 1).

---

[1] See p 204

[2] The effects of the JVs and acquisitions surveyed in the present study on competition and industry structure are discussed on pp 198-202.

By far the largest proportion of these is accounted for by share purchases, which increased their share from 952 operations (58%) to 1,905 (79%) over the period; the share of JVs has halved, from a third of the total to 15%.

The growth in the total is due largely to the huge increase in national operations - some 172%, with share purchases increasing from 384 to 1,402 cases (60% to 81%) and the shares of takeovers and mergers and JVs, although growing in absolute terms, falling from 21% - 8% and 19% - 11% respectively.

As far as takeovers are concerned, purchasing the majority of a company's capital does not necessarily give full control; depending on the proportion purchased, minority shareholders may still possess blocking rights - that is, the right to prevent decisions being made. The percentage of shares required for full control varies from country to country. On the other hand, control may be achieved at levels under 50%, depending on how widely dispersed the share ownership of the company concerned is. In addition, a company may be taken over in instalments, so that a small purchase of shares may result in full control being acquired. Because of the variations in national laws, then, the Commisssion classifies all international takeovers, mergers and share purchases as share purchases. That is, the purchase of 100% of the capital of a French company by a British firm counts as a share purchase, not as a takeover.

The number of international operations has actually dropped considerably. New JV numbers in particular have fallen steadily, and by 1980 stood at only 40% of their 1973 level. JVs accounted for only 26% of international operations in 1980, compared with 43% in 1973. This fall meant that by 1980 international JVs were outnumbered by their national counterparts.

Similarly, by 1980 only 26% of new share participations in the EEC were international operations, compared with 60% in 1973. This is due to a 265% rise in the number of national operations rather than to any drastic fall in the number of international share participations.

TABLE 1

NATIONAL AND INTERNATIONAL OPERATIONS IN THE E.E.C.

YEAR	TOTAL TAKEOVERS AND MERGERS		TYPE OF OPERATION						BREAKDOWN OF OPERATIONS BY NUMBER OF FIRMS INVOLVED	
			SHARE PURCHASE		JOINT VENTURES		TOTAL			
	No. of operations	No. of firms involved	No. of operations	No. of firms involved	No. of operations	No. of firms involved	No. of operations	No. of firms involved	Bilateral operations	Multilateral operations
1973	138	318	952	1989	548	1476	1638	3783	1298	340
1974	165	404	1018	2241	552	1615	1735	4260	1367	368
1975	231	548	1500	3221	550	2201	2281	5970	1871	410
1976	136	324	1346	2880	575	1891	2057	5095	1639	418
1977	146	383	1692	3637	482	1609	2320	5629	1948	372
1978	137	315	1727	3655	440	1235	2304	5205	1988	321
1979	146	319	2342	4917	439	1434	2927	6670	2532	395
1980	148		1905		366		2419		2061	358
NATIONAL OPERATIONS										
1973	138	318	384	836	119	478	641	1632	544	97
1974	165	404	607	1293	151	509	923	2206	789	134
1975	231	548	1118	2356	237	1157	1586	4061	1387	199
1976	136	324	977	2102	213	785	1326	3211	1137	189
1977	146	383	1279	2688	194	739	1619	3810	1440	179
1978	137	315	1328	2763	162	540	1627	3618	1465	161
1979	146	319	1824	3793	216	799	2186	4911	1936	250
1980	148		1402		191		1741		1506	235
INTERNATIONAL OPERATIONS										
1973	-	-	568	1153	429	998	997	2151	751	246
1974	-	-	411	918	401	1106	812	2024	578	234
1975	-	-	382	865	313	1044	695	1909	484	211
1976	-	-	369	778	362	1106	731	1884	502	229
1977	-	-	413	949	288	870	701	1819	508	193
1978	-	-	399	892	278	695	677	1587	524	160
1979	-	-	518	1124	223	635	741	1759	596	145
1980	-	-	503		175		678		555	123

Source : EC Commission, Fourth - Eleventh Reports on Competition Policy, Brussels & Luxembourg, April 1975 - April 1982.

ii) Regional Distribution.

Table 2 shows how these international operations are split between those involving Community firms exclusively and those involving firms from non-member countries (NMCs), either exclusively or in combination with Community firms.

With the number of share purchases involving NMC firms growing steadily since 1976, the proportion involving Community firms exclusively has dropped, after a brief revival in 1979, to only 45% of the total.

The number of international JVs in the EEC has shown a steady fall over the period, and this has been particularly pronounced in the numbers involving Community firms exclusively. Only 74 of these took place in 1980, showing a drop of 45% on the 1979 figures, which had themselves been following a steady declining trend. Thus in 1980 only 42% of the JVs taking place in the Community involved EEC firms exclusively.

As a whole, then, the proportion of total international operations recorded by the Commission involving Community firms exclusively had fallen to 44% by 1980. The total number of operations in 1980 was 32% below the 1973 level, with internal EEC operations being 47% below their 1973 level.

From their involvement in 55% of the share purchases and 58% of the JVs in 1980, firms from non-member countries can be seen to have made considerable inroads into Community markets.

Table 3 shows that France led the way in international operations in 1980, with 23% of the total being located there. The UK and West Germany followed closely behind, with 22% and 19% respectively. These three countries thus accounted for 64% of the recorded international operations in the Community in 1980.

TABLE 2

INTERNATIONAL OPERATIONS IN THE EEC - OPERATIONS INVOLVING EEC FIRMS ONLY AND OPERATIONS INVOLVING NON-COMMUNITY FIRMS.

YEAR	TYPE OF OPERATION								
	SHARE PURCHASE			JOINT VENTURES			TOTAL		
	EC[1]	NMC[2]	TOTAL	EC	NMC	TOTAL	EC	NMC	TOTAL
NUMBER OF OPERATIONS :									
1973	340	228	568	233	196	429	573	424	997
1974	234	177	411	207	194	401	441	371	812
1975	200	182	382	173	140	313	373	322	695
1976	198	171	369	165	197	362	363	368	731
1977	202	211	413	138	150	288	340	361	701
1978	187	212	399	166	112	278	353	324	677
1979	273	245	518	135	88	223	408	333	741
1980	227	276	503	74	101	175	301	377	678
AS PERCENTAGE OF TOTAL :									
1973	60	40	100	54	46	100	57	43	100
1974	57	43	100	52	48	100	54	46	100
1975	52	48	100	55	45	100	54	46	100
1976	54	46	100	46	54	100	50	50	100
1977	49	51	100	48	52	100	49	51	100
1978	47	53	100	60	40	100	52	48	100
1979	53	47	100	61	39	100	55	45	100
1980	45	55	100	42	58	100			

EC = OPERATINS INVOLVING COMMUNITY FIRMS EXCLUSIVELY.

NMC = OPERATIONS INVOLVING FIRMS FROM NON-MEMBER COUNTRIES, EITHER EXCLUSIVELY OR IN COMBINATION WITH COMMUNITY FIRMS.

Source : EC Commision, Fourth - Eleventh Report on Competition Policy, Brussels & Luxembourg, April 1975 - April 1982.

TABLE 3

REGIONAL DISTRIBUTION OF INTERNATIONAL OPERATIONS IN THE EEC. (%)

YEAR	FEDERAL REP. OF GERMANY	FRANCE	ITALY	NETHERLANDS	BELGIUM	LUXEMBOURG	UNITED KINGDOM	IRELAND	DENMARK	TOTAL EEC
1966	22	19	13	16	24	6				100
1970	24	22	12	13	22	7				100
1971	22	24	11	12	24	7				100
1973	14	22	6	11	19	14	12	1	1	100
1974	22	22	7	8	16	7	16	1	1	100
1975	20	20	4	7	21	9	15	3	1	100
1976	23	16	5	8	25	8	11	2	2	100
1977	23	14	3	10	19	8	16	5	2	100
1978	20	15	4	10	18	6	21	6	-	100
1979	14	19	6	10	17	7	21	5	1	100
1980	19	23	5	9	12	5	22	5	-	100

Source : EC Commission, First - Eleventh Reports on Competition Policy, Brussels & Luxembourg, April 1972 - April 1982.

iii) Industrial distribution.

Table 4 gives a breakdown by industry of the international operations recorded by the Commission within the EEC, and shows that the highest number of operations is that of the metal-using industries, with a 29% share in 1980. There are two possible reasons for the high number of service undertakings : a) as firms become more international in their outlook, service industries feel the need to be better represented abroad; b) service 'products' are subject to greater regulation and administration than industrial ones, and in many cases it helps to have the assistance of an on-the-spot partner.

Other statistics are provided by the Business Co-operation Centre. This is a branch of the Commission set up to promote transnational business collaboration in the EEC by attempting to find partners for applicant firms. The statistics[1], in Tables 5 and 6, indicate that the largest share of activity is taken up by the metal-using industries, which together accounted for almost 40% of the Centre's work between 1973 and 1980. Mechanical engineering took 20% of the total. The Centre's work is weighted towards smaller firms, being aimed primarily at firms employing between 50 and 400 persons[2]. Tables 5 and 6 do not show any trend over time, and to do so would perhaps be misleading; these were the first seven years of the Centre's existence, and the growing amount of business passing through its office every year may be attributable more to growing public knowledge of it than to any increased demand for international business co-operation.

---

1 The statistics, taken from the Centre's annual reports, record enquiries circulated among its contracts for partners (Table 5) and replies received (Table 6). See also pp. 13-14 And Appendix 1.

2 Although the Centre's work is biased towards smaller firms, there is no reason to suppose that the proportions of its work accounted for by the various industries should differ substantially from the distribution of the unknown number of total transnational operations in the EEC.

TABLE 4

INTERNATIONAL OPERATIONS IN THE EEC : BREAKDOWN BY INDUSTRY (%)

YEAR	METAL-USING INDUSTRIES	ENERGY	CHEMICALS	TEXTILES	OTHER MANUFACTURING INDUSTRIES	FOOD INDUSTRY	SERVICES	TOTAL
1966	43	3	15	6	12	3	18	100
1970	36	1	11	6	13	7	26	100
1971	39	1	11	5	14	5	25	100
1973	27	2	8	4	11	9	39	100
1974	21	3	9	4	9	4	50	100
1975	28	2	9	4	14	7	36	100
1976	27	2	9	5	15	8	34	100
1977	27	2	9	5	16	8	33	100
1978	32	2	8	5	17	8	28	100
1979	30	3	7	5	22	8	25	100
1980	29	4	10	6	15	8	28	100

Source : EC Commission, First - Eleventh Reports on Competition Policy, Brussels & Luxembourg, April 1972 - April 1982.

TABLE 5

WORK OF THE BUSINESS CO-OPERATION CENTRE : Information requests 1.11.73 - 31.10.1980.

Source : First - Eighth Annual Reports of the Business Co-operation Centre, Commission of the European Communities, Brussels, 1974 - 1981.

	B	G	DK	F	GB	I	IRL	L	NL	Non-Member Countries	TOTAL	
Requests for Information	254	584	89	588	1172	548	110	10	138	431	3924	
Circulated Enquiries for Partners												%
Extractive Industries	1			2						2	5	0.68
Chemical Industry	3	12	1	22	26	19	3	-	7	8	101	13.74
Metal Structures	7	13	1	22	25	11	6	2	2	9	98	13.33
Mechanical Engineering	9	25	2	35	36	16	2	-	7	16	148	20.14
Electrical Engineering	3	5	1	6	18	7	1	-	-	3	44	5.99
Food Industry	2	10	1	4	3	9	6	-	6	1	42	5.71
Textiles	-	3	1	4	1	3	1	-	1	4	18	2.45
Clothing	1	1	1	10	4	5	8	-	2	-	32	4.35
Wood	2	7	1	6	4	10	3	-	1	3	37	5.03
Paper	3	7	1	5	4	3	-	-	3	3	29	3.95
Misc. Industries	-	1	-	-	1	1	-	-	-	-	3	2.41
Building & Civil Engineering	2	4	1	6	7	6	1	-	3	2	32	4.35
Commerce	8	5	-	8	6	-	-	-	4	2	33	4.49
Transport	3	2	4	4	10	1	-	-	4	-	28	3.81
Services	10	6	4	17	28	5	1	-	11	3	85	11.56
TOTAL	54	101	19	151	173	96	32	2	51	56	735	100.0

TABLE 6

WORK OF THE BUSINESS CO-OPERATION CENTRE : Replies received 1.11.1973 - 31.10.1980

Source : First -Eighth Annual Reports of the Business Co-operation Centre, Commission of the European Communities, Brussels, 1974 - 1981.

No. of replies received	B	G	DK	F	GB	I	IRL	L	NL	Non-Member Countries	TOTAL	%
Extractive Industries	2	11	-	7	6	-	-	-	1	1	28	0.36
Chemical Industry	210	385	23	125	291	72	18	2	83	9	1218	15.52
Metal Structures	175	357	33	189	233	63	27	6	91	9	1183	15.08
Mechanical Engineering	177	410	33	314	418	94	26	1	135	18	1626	20.72
Electrical Engineering	40	101	9	45	84	18	2	-	12	15	326	4.16
Food Industry	35	135	21	38	89	19	8	1	32	1	379	4.83
Textiles	25	40	-	26	25	9	4	-	13	1	143	1.82
Clothing	36	82	3	47	36	51	8	-	12	3	278	3.54
Wood	32	51	2	80	56	17	5	-	15	3	261	3.33
Paper	32	40	1	48	58	12	7	3	32	1	234	2.98
Misc. Industries	1	12	1	14	3	1	-	-	-	-	32	0.41
Building & Civil Eng.	56	69	12	38	69	23	8	1	32	-	308	3.93
Commerce	49	100	11	135	222	103	4	4	39	10	677	8.63
Transport	30	49	10	39	52	13	-	-	24	2	219	2.79
Services	104	260	23	146	181	103	11	3	90	13	934	11.90
TOTAL	1004	2102	182	1291	1823	598	128	21	611	86	7844	100.00

CONTACTS ESTABLISHED : 605

- The promotion of co-operation and the Business Co-operation Centre :

In its memorandum of 1970 on a common industrial policy for the European Community[1], the Commission suggested, inter alia, that it should actively promote co-operation by operating a 'marriage bureau' to bring firms together, in order to increase their competiveness and help them to adjust to the expanded market.

The Business Co-operation Centre was set up in Brussels in 1973 for this purpose. Unfortunately, despite the great response which it has had from companies both inside and outside the Community, the Centre has been run down in recent years. Whereas a member of the Centre's staff used to visit a company which had applied for a possible co-operation, this is no longer possible. These meetings were very valuable, especially since many firms did not know the correct way in which to go about such an application. Many of them were not specific about exactly what they wanted, and even less so about what they could offer in return. The meetings were designed to pinpoint these matters, and left the firms concerned in a much clearer frame of mind. The Centre is thus unable to offer as effective a service as it would like.

The document BRE/30/75-E, produced by the Business Co-operation Centre, and which gives an overview of its aims, is contained in Appendix 1.

Some of the Centre's work is in fact now being carried out by national organisations - notably the West German engineering employers federation, the VDMA, and a group of Chambers of Commerce in the Netherlands. Organisation such as this on a national scale may well be more efficient than a central office in Brussels. It would, for example, be much easier to visit the firms, and would also result in a larger organisation overall, since effective co-operation on a European scale by the various national organisations should result in a larger and more efficient network.

---

[1] Commission of the European Communities, 'Memorandum on Industrial Policy', Brussels, March 1970.

Attention is focussed on small and medium-sized enterprises because it is assumed that the larger firms can more easily afford their own economists, lawyers and accountants to solve their own problems.

Appendix 2, on Commission regulations, contains details of agreements which are excluded from the strictures of Article 85(1) (also in Appendix 2) and which are therefore permitted.

CHAPTER ONE

PREVIOUS LITERATURE ON JVs[1].

The literature is considered under the following headings :

1. Definitions ;
2. Types of operation ;
3. Industries covered ;
4. Methodology ;
5. Economic benefits and justifications of JVs ;
6. Anticompetitive effects of JVs ;
7. Motives for entering JVs ;
8. Weaknesses of previous studies and the development of the present study.

1. Definitions

At the outset, it should be noted that there is some difficulty in defining the term 'Joint Venture' precisely. Most commentators use the definition provided by Backman : "A joint venture is the creation of a new business organisation which is owned by two or more enterprises".[2] This gives great flexibility in terms of the ownership structure, so that a 50:50 and a 90:10 structure both come equally under the heading. This is the 'equity JV'. Another type of JV, excluded from the above definition, is the 'contractual JV', which is "a special combination of one or more persons where in some specific venture, a profit is jointly sought without any actual partnership or corporate designation".[3] The basic characteristic of this type of venture is that "investment and expenses are divided between the partners according to fixed percentages".[4]

---

1 This chapter concerns literature on the effects of co-operation upon the structure of the industry. Literature on corporate strategy is discussed in Chapter 3.

2 J.Backman p.7 (see Bibliography for full reference for this and other cited studies). See also E.C. Commission definition, p 58.

3 W.G. Friedman, p.58

4 Ibid., p.59

Edstrom offered three alternatives for the equity JV :

i) an acquisition of up to 50% of another company;

ii) two companies each extract some activities and form a new, jointly - owned company to manage them, while keeping the original companies basically intact ;

iii) two companies jointly buy a third company.

However, having defined an acquisition as "when one company has acquired at least 50% of all assets and liabilities of another firm", Edstrom admits that "the borderline between an acquisition and an equity JV is unclear in practice".[5]

2. Types of operation

The literature is almost entirely concerned with domestic JVs in the USA. See, for example, Backman, Boyle, Friedman & Berg, Friedman, Berg & Duncan, Hlavacek & Thompson, Mead and Pfeffer & Nowak. Asch & Seneca also wrote about US ventures, but these were illegal collusions rather than JVs as such. Edstrom too wrote about national ventures, for both acquisitions and JVs, but these were Swedish. Gullander wrote about Swedish domestic JVs and international JVs in European industrialised countries involving at least one Swedish firm.

The present study looks at cross-frontier collaborations in the EEC, including both joint ventures and acquisitions, involving one British company in each case.

3. Industries covered

Most of the studies look at manufacturing industry in general. Mead looked at joint bidding behaviour in oil and gas resource markets and Hlavacek & Thompson considered technology based industries. Backman and Friedman & Berg studied the chemical industry, with Friedman, Berg & Duncan adding resource processing and engineering in comparative studies.

---

[5] Edstrom, p.480.

(3 continued....)

Backman wrote that the JV has become increasingly important in the chemical industry, on account of "the necessity for diverse technical abilities and special knowledge in new fields of proposed activity. The use of JVs has been most extensive for petrochemicals..... ...The technical problems involved, the high costs for research and development, and the various time lags before a profitable return could be earned have made petrochemicals a suitable area for sharing capital expenditure".[1]

Friedman & Berg, in concentrating on chemicals, touched on the benefit, and a potential problem, in isolating one industry for analysis : "interpretation is clouded by neither differential industry technological opportunities nor by inter-industry market structure effects. Unfortunately, the gain in precision from reliance on a single industry carries the danger of this industry being atypical".[2]

The present study has also confined itself to one industry - mechanical engineering - in order to avoid variations due to different industry characteristics.

4. Methodology

A number of the studies used an analysis of published data at the firm level. Asch & Seneca looked at 51 firms found guilty of collusion under the US Sherman Act, plus a control group of 50 non-collusive firms drawn randomly. Others to use published data at that level were Boyle; Friedman & Berg ; Friedman, Berg & Duncan; Mead; and Pfeffer & Nowak. Boyle complained that since most JVs are privately held, the necessary data on them is not generally available from public sources.[3] Edstrom's analysis was at the industry

---

1 Backman, p.p. 14-15

2 Friedman & Berg, p.1330

3 Boyle, p.81

(4 continued...)

level, and he admitted its weakness : "The reason for using industry data instead of data for individual firms is the difficulty in obtaining comparable data for individual companies. The use of industry data makes any generalisation about the behaviour of individual firms problematic. If we are willing to accept that the firms engaged in acquisitions, that contractual and equity JVs are typical for their industry, then generalisations are justified, but we have no assurance of this".[1] Backman did no detailed statistical analysis.

It should be noted that only Gullander and Hlavacek & Thompson carried out personal interviews with JV managers. The latter study concentrated on 19 new-product JVs, whose formation had been publicised. Gullander added his series of interviews with top executives of 40 JVs involving at least one Swedish firm each to an extensive literature search on JVs in Europe.

The present study also uses the personal interview method, details of which are discussed in Chapter 5.

5. Economic benefits and justifications of JVs

Mead has pointed out that joint ventures may be justified as being "the best means available of obtaining entry in an industry or geographic market",[2] and considered four justifications :

a) Absolute capital requirements, due to large scale production, may be so high that only a few firms are potential entrants separately;[3]

---

1 Estrom, p.479

2 Mead, p.823

3 See also p.p. 66 and 99.

(5 continued...)

b) Risks associated with entry and operation in a given industry or geographic market may be so great that few or no existing firms are able or willing to assume such risks alone ;

"It should be noted", wrote Mead, "that points a) and b) are both justifications in terms of increasing competition in the industry entered whereas the normally expressed fears are that JVs reduce competitive vigour".[1]

c) Separate operations may be economically wasteful as a means of performing some necessary function ;

d) A JV may be justified where a large investment is expected to produce important external economies that accrue indiscriminately to firms in a given industry, rather than primarily to the investing firm - it may, for example, produce non-patentable processes and information that quickly becomes public property.[2]

Mead rejected two additional justifications - the argument in favour of "complementary and overlapping" technology because "the new technology may be hired in the relatively free market for technologists"; and Backman's argument that "the partners are able to diversify their activities with a smaller investment than would be required if either one undertook the project alone"[3] because, claimed Mead, this "assumes that there are welfare benefits which follow from increased diversification" and that "this argument is the opposite of the specialisation and division of labour thesis and is yet to be established".[4]

But there may undoubtedly be benefits from diversification. It may reduce dependence on one product or geographic market, for example, and thus reduce the risk factor. And in the ICI - Montedison JV[5] in 1977, if the firms had independently

---

1 Ibid, p.824
2 Ibid, p.p. 824-5
3 Backman, p.8
4 Mead, p. 825
5 See p. 66.

built factories for the production of aniline for their own use, they would each have been left with substantial excess capacity at the cost of a very heavy investment. But a factory between them would have just met their joint requirements, with a substantial saving resulting to both companies.

Moreover, Friedman & Berg stated that their results were "consistent with Backman's view that complementary/ overlapping technologies play an important role in JVs by chemical firms".[1]

Backman added further economic benefits : "The JV permits the sharing of technology as well as managerial talent.....Research and development activites may be broadened. Sales outlets may be obtained or the supply of raw materials may be assured. Economies in purchasing, selling, handling and in other areas may be derived..... .....Finally, in terms of its broader economic impact, the JV adds to the number of actual competitors and to total capacity in the market and as a result often brings new vigour to competition for the products and markets involved".[2]

6. Anticompetitive effects of JVs

Mead also included three possible anticompetitive effects of JVs :

i) Restraint of competition between horizontally related firms;

ii) Foreclosure of markets; that is to say, in the case of a vertical relationship a JV may exclude competing independent suppliers from dealing with the parent organisations.

iii) Reduction in potential competition. Pfeffer & Nowak wrote that the JV "may preclude the independent entry into the market by both firms, or may forestall entry by another firm. And, horizontal JVs may raise industry barriers to entry by providing the joint subsidiary with financial and technical resources that would not be available to independent firms attempting to enter the market."[3]

---

1 Friedman & Berg, p.1336
2 Backman, p.8 See also the present study, p.200.
3 Pfeffer & Nowak, p.323

7. Motives for entering JVs

Pfeffer & Nowak argued that JVs "are undertaken by firms to manage their competitive and buyer-seller interdependence, and that JVs, if successful in reducing the uncertainty associated with these forms in interdependence, are simultaneously successful in reducing competition in the market place."[1]

They formulated two hypotheses :

a) For vertically related industries, JVs are undertaken "to manage the buyer-seller interdependence, with the greater the interdependence, the greater the proportion of JVs undertaken with partners in that industry".[2]

b) In horizontal relationships, JVs "are undertaken not to control buyer-seller interdependence, but rather to overcome competitive interdependence. Therefore we argue that within industries, JV activity will be more strongly related to industry structure as measured, for example, by industrial concentration".[3]

They wrote that "the general advantage of managing interdependence is the reduction of uncertainty"[4] and noted that it has been argued[5] that firms seek to reduce uncertainty and will even trade off profits for certainty. In the case of vertical interdependence, "the advantages include ensuring a stable and predictable source of supply of important materials or components, or ensuring reliable outputs and markets for the product".[6]

Pfeffer & Nowak hypothesised that at very low levels of concentration "horizontal JVs would have only a limited impact in reducing competitive uncertainty because there are

---

1 Ibid, p.316
2 & 3 Ibid, p.329
4 Ibid, p.332
5 Richard E.Caves, "Uncertainty, Market Structure and Performance: Galbraith as Conventional Wisdom", in J.W.Markham & G.F.Papanek (eds.) 'Industrial Organisation and Economic Development', Boston, Houghton Mifflin, 1970, pp. 283-302.
6 Pfeffer & Nowak, p. 332

numerous firms that must be organised".[1]. Where there are very few firms in the industry, such JVs may not be necessary to manage competitive interdependence, where other less formal forms of co-ordination may be adequate. Thus JV activity will be highest at intermediate levels of concentration. Their results supported these contentions, showing that JV activity is indeed highest at intermediate levels. "It should be noted", they wrote, "that the difference in concentration variable alone accounts for 30% of the observed variation in the proportion of horizontal JV activity."[2]

The results of the investigations into vertical relationships indicate that even more of the variance in the pattern of JV activity is accounted for by resource interdependence variables than in the formation of JVs. Pfeffer & Nowak claimed that : "These results further support the argument we have developed. Joint subsidiaries are formed more often in industries which are vertically related to the industry of the parent firms. The fact that the concentration ratio for the industry of the joint subsidiary is much less important in accounting for the pattern of JVs indicates that JVs generally do not represent diversification into oligopoly markets by the parent firms, and that joint subsidiaries are not being extensively employed to enter (and thereby introduce competition to) highly concentrated industries."[3]

Pfeffer & Nowak concluded that the results are consistent with the idea that JVs are used to manage interfirm inter-dependence, and that they are simultaneously successful in reducing competition in the market place.

---

1 Ibid, p.330
2 Ibid, p.331
3 Ibid, pp 336-337. The present study uses both subjective concentration measures and direct questions on the importance of competition in preference to concentration ratios (see pp. 166-67).

TABLE 7 Pfeffer & Nowak : Vertical relationships and JV activity

Variable	CORRELATION A	B
Proportion of industry i's sales to industry j	.28*	.27*
Proportion of industry i's purchases from industry j	.25*	.42*
Proportion of industry i's total transactions with industry j	.28*	.39*
Concentration ration in industry j	.16**	.10***
Proportion of total employment engaged in R & D in industry j (1)	.25*	.16**

* $p < .001$ ** $p < .05$ ***$p < .10$

(1) The proportion of total employment engaged in R & D is used as a measure of technological intensity.

A : Correlations of JV activity with interdependence and industry structure variables.

B : Correlations of the proportions of industry i's joint subsidiaries in industry j with industry structure variables.

Source : Pfeffer & Nowak, pp333 & 336

Friedman, Berg & Duncan were rather more cautious about Pfeffer & Nowak's results : "These conclusions warrant more careful study. From the evidence they (Pfeffer & Nowak) present, one could argue that rivalry promotes time-economising activity, since a relatively competitive market structure puts a premium on early introduction of new products."[1]

It is also possible that at intermediate levels (ie, where the smaller firms have not yet been squeezed out of the market) smaller firms may use JVs either with different large firms in a defensive balance (as suggested by Gullander, I) or with each other in order to survive against the very large competitors.

Another possible reason for JVs taking place in highly concentrated industries might be that the concentration ratio may reflect minimum efficient scale and JVs may be the chosen means of obtaining available economies of scale.[2]

Mead, writing in 1967 on joint bidding agreements for oil and gas leases in Alaska and the Gulf of Mexico between 1959 and 1965, examined the behaviour of 16 firms in Alaska and 14 in Mexico which had bid separately following the break-up of an agreement. He found that only one of the Alaskan firms, and two of the Mexican firms, had bid more frequently against former partners than non-partners within two years of the break-up. This represented deviations from the expected frequencies which were too great to be explained by chance, using a 0.01 level of significance.

He found, however, that the tendency toward restrained bidding between former partners disappeared over the following two-year period, and in addition, that bidding partnerships in one geographical area have no effect on bidding behaviour in another area.

---

1 Friedman, Berg & Duncan, p.103

2 A.Millington, Centre for European Industrial Studies at the University of Bath, internal discussion paper, 'Domestic JVs', 1981 (unpublished).

TABLE 8

Mead: Analysis of Bidding Conflict and Frequency, Alaska & Gulf of Mexico

	Alaska Period following termination of agreement		Gulf of Mexico Period following termination of agreement	
	First 2 years	Second 2 years	First 2 years	Second 2 years
No. of former partners bidding against anyone	16	9	14	4
No. bidding more frequently against former partners than against non-partners	1[a]	3[b]	2[a]	5[b]
No. bidding less frequently against former partners than against non-partners	15[a]	6[b]	12[a]	9[b]
No. not bidding against former partner				
Frequency of bidding against average non-partners	3.4	2.5	2.5	3.1
No. bidding against both partners and non-partners	11	7	9	11
Frequency of bidding against former partners	3.6	13.8	2.7	8.5
against non-partners	10.1	7.7	5.6	8.1

[a] Actual frequencies deviate from expected too far to be explained by chance, using a 0.01 level of significance.

[b] The deviation of actual frequencies from expected could be due to chance, using a 0.01 level of significance.

Source : Mead, p.843

Mead also discovered that joint bidding arrangements can lead to serious distortions in pricing. His data show that the high bid is a positive function of the number of bidders in both Alaska and the Gulf of Mexico, as shown by simple regression analysis :

ALASKA $\quad \text{Log } Y = .48529 + 1.28707 \text{ Log } X \quad R^2 = .31$
$\qquad\qquad\qquad\qquad\qquad\qquad\qquad\qquad\qquad\qquad (0.05416)$

GULF OF MEXICO $\quad \text{Log } Y = 1.59697 + 1.35197 \text{ Log } X \quad R^2 = .43$

where Y is the highest bid and X is the number of bidders.

However, Mead's conclusion of causality in the bid price does not necessarily follow. It could well be (and very likely is) the case that more people will bid for a more attractive plot of land, and that it is the attractiveness of the plot, and not the number of bidders, which causes the highest price.

Boyle also looked at the competitive position of the JV vis-a-vis its parent companies and the nature of the competitive relationship between the parent companies.

As far as the former goes, Boyle found that 55% of the parent companies were classified in the same two-digit industry group as their subsidiaries, and that 44% manufactured products in the same 4-digit industry as that of their subsidiary. Since his data show that 85% of the non-horizontal relationships between parents and subsidiaries involve some form of vertical integration, "looking at the entire group it appears that the parent companies and the subsidiaries manufactured products in completely unrelated areas in less than 10% of the cases".[1]

---

1 Boyle, p.88 For a comparison with the present study, see p 164.

Analysis of the competitive relationships between the parents showed that "in about 55% of the cases, two or more of the parent companies were direct competitors in the production and sale of one or more products" (on a 5-digit product class basis).[1] Although Boyle admits that "this type of analysis has one major shortcoming, however; because estimates are not available of the dollar value of sales in each product class, it is impossible to obtain quantitative measures of the exact extent to which the parent companies are in competition with each other",[2] he claims that his data do suggest that more than one-half of the 276 joint subsidiaries included in his analysis (which he states represents a minimum of the domestic joint subsidiaries of the 500 largest US manufacturing corporations) "present at least one of the basic ingredients apparently necessary for a successful prosecution under Section 7 (of the US 'Clayton Act'), namely, the fact that the parent companies are competitors."[3]

Boyle concluded that these parent companies "seem to be using the joint subsidiary as a means of increasing the existing integration between their presumably independent companies (a fact that suggests the importance of the joint subsidiaries may far exceed their actual size)."[4]

Backman took up the three arguments presented against joint ventures in terms of their effect on the market that they :

1) tend to limit the present and potential competition in the product market affected ;
2) tend to result in domination of the product market because of the economic power of the parent companies; and
3) tend to lessen competition in other product lines in which the two companies are already competing

- and rejected them all.

1,2 Boyle, p.89
3 Ibid, p.90
4 Ibid, p.92

Writing about the chemical industry, Backman rejected the first argument on the grounds that : "The fear that JVs may reduce potential competition ignores the possibility that neither company may be willing to enter the market on an individual basis and hence that in the absence of JVs the number of competitors will be fewer, not greater. Chemical companies are not looking for partners simply to share profits. Rather, JVs are formed because there are advantages to both partners and thus make possible the entry of a new firm or the development of a new product. It is probable that in the absence of the JV, a new entry otherwise would not have taken place in many instances.

"The basic factor affecting decisions to enter a market is the prospective economic development of a new product. Where a demand levels off, the incentive to enter a market may become zero. On the other hand, where strong growth is in prospect, the incentive for new entry is increased accordingly. It is not the existence of a JV which inhibits entry in the static situation, nor will it prevent entry where dynamic growth is anticipated. The role of the JV is subordinate to this fundamental economic order."[1]

A new joint venture will, said Backman, affect existing competition insofar as in a static market the JV can only gain a market share at the expense of existing companies. But in an expanding market both the JV and its competitors can grow in absolute terms, although relative shares will change.

This situation of course applies to <u>any</u> venture, from a greenfield venture to an expansion of existing operations. In any situation in which one firm increases its relative market share, at least one other firm must lose a share. This is the effect of <u>increased</u> competition and the greater competiveness of one (the growing) firm. As Backman commented : "Competition is dynamic, not static."[2]

---

1 Backman, pp16-17
2 Backman, p.18

Competitiveness and efficiency can say more about competition than the number of firms in the market. In theory, as firms are eliminated from the market the remaining firms can adjust to take advantage of their increasingly dominant positions. Hence the best protection of competition is simply the elimination of barriers to entry and re-entry.

Backman refuted the second argument on the grounds that "there has been considerable entry into many chemical markets despite the organisation of JVs."[1] He then mentioned several others which, he claims, also indicate that market dominance is neither the result not the objective of JVs : "First, the areas marked by the prevalence of JVs have been markets in which the existing firms are large ones. Secondly, the parents are not acquiring an existing firm but almost invariably are creating a new competitor. Thirdly, despite their large resources, the parents commit limited resources to the JV and both parents usually must be in agreement if these amounts are to be increased. Moreover, because of their size both parents usually have large competing demands from other activities upon their limited (rather than unlimited) resources. Finally, JVs often provide for research and development as a key element in their plants, thus indicating that economic growth in terms of new and better product lines, rather than market foreclosure, is the primary motive in their formation."[2]

Backman rejected the third argument on the grounds that : "Each company is under pressure, regardless of its corporate relationships in special areas, to compete vigorously in all markets in order to justify the investment required for the manufacture of each of its product lines. Anti-competitive behaviour should not be inferred in all markets because of a business relationship in one market. Such an approach is based one guilt by association rather than proof of anticompetitve behaviour." 3

---

1 Ibid, p22
2 Ibid
3 Ibid, p.23

Backman suggested[1] a number of competitive effects of JVs on an industry which could be measured, namely :

1) Subsequent changes in the number of competitors, in capacity, and/or output, are existing producers forced out of the market ?
2) Countermeasures taken by existing producers :
   a) Intensify their research and development and/or develop improved or new product lines ;
   b) Improve services ;
   c) Intensify selling by adding to sales force, by increasing advertising budgets, or by other means ;
   d) Modernise their own capacity to lower costs or to improve quality ;
   e) Improve credit terms.
3) Changes in market shares.
4) Impact on prices and price practices - for example, after one particular US chemicals JV was formed,a competitor offered customers five-year contracts with guarantees against price increases and the benefit of any price cuts.
5) Are other firms able to enter the industry ?

Of course, where a JV is formed between two existing producers, it may prevent at least one of them from being forced out of the market, if the purpose of the JV is to ensure survival. Moreover, although the occurence of countermeasures may at first sight appear to be a response to the JV, they could just be due to a relative decline in the industry itself, which would force such measures as producers struggle to retain their absolute market share (ie, to increase their relative share of a shrinking market). JVs may simply be another response to this decline, or else just another means of achieving the same countermeasures.

Backman wrote that JVs should have no more effect on market entry than any other company of similar size and resource. He concluded : "These illustrations also underline the importance of examining each JV within the framework of its own market experience. Any per se approach which attempts to bar JVs would result in anticompetitive effects in many markets in the

---

1 Ibid, p14. The absence of a control group & the limited size of the present study meant that these effects could not be tested (see p.46).

name of promoting competition."[1]

Edstrom also wrote about industrial concentration, concluding that "industry concentation and financial strength are important determinants of both acquisition and JV behaviour while differences in corporate goals and the characteristics of the other party in the relationship account for variations in behaviour."[2]

He examined the following four hypotheses :

1) High industry concentration will lead to a high relative propensity to acquire other firms and to engage in co-operation. This effect ought to be more pronounced at higher levels of concentration ;
2) Firms acquire profitable and fast growing firms ;
3) Acquisitions will generally be more closely associated with financial strength than equity JVs, and equity JVs more closely than contractual Jvs;
4) Acquisitions will be used against firms which are financially weak while contractual and equity JVs will be used in relations with firms of equal financial strength.

Edstrom defined an acquisition as the purchase by one company of at least 50% of all assets and liabilities of another firm, though he admitted that the borderline between an acquisition and an equity JV is unclear in practice.

Being based on an analysis of Swedish manufacturing industry and hence freed from the antitrust restrictions which bind the US cases, Edstrom's analysis can be expected to be somewhat closer to the case in the EEC - though like his American counterparts Edstrom too concentrated on national operations.

Edstrom's results indicated that acquisitions are more common within the same industry sector while contractual JVs occur

---

1 Ibid, p.23
2 Edstrom, p.477

most often between industry sectors in manufacturing (ie, vertical relationships) and equity JVs are weighted towards relationships between manufacturing and other industries - ie, conglomerate arrangements. "The use of equity JVs in relationships involving firms outside manufacturing may indicate a need to complement existing know-how within the firm."[1]

Edstrom found that the most common functional areas for equity JVs are in production and marketing, with 44% and 40% respectively of the total, and that joint production is to a large extent concentrated on new products.

A breakdown of contractual JV activity showed 38% in marketing, 27% in product development, 22% in production and 13% in supply, showing relatively more JVs in product development and supply and relatively less in production compared to equity JVs.[2]

"Even though there is a variation among individual acquisitions, equity and contractual JVs," he wrote, "the choice of strategy seems to vary with industry linkage and the size of the firms involved."[3]

TABLE 9

Edstrom: Classification of strategy according to industry linkage

Strategy	With the same industry sector %	Between industry sectors in manufacturing %	Before manufacturing and other industries %
Acquisitions	45	34	21
Equity JVs	20	31	49
Contractual JVs	31	45	24

Source : Edstrom, p.489

Edstrom drew the following conclusions[4] from his results :

- Industry concentration provides a source of contingencies and uncertainty for firms in that industry which they try to

---

1 Ibid, p.489. See also p. 164 of the present study for a comparison of results.

2 Edstrom, p.487

3 Ibid, p. 489

4 Ibid, pp 489-90

avoid or control, eg., through acquisitions and co-operation.

- Adaptive strategic actions require resources. The lack of important resources such as financial resources will restrict a firm's strategic action. The need for resources varies with type of strategic behaviour.
- The use of acquisitions tends to vary with the nature of strategic change and hence with the size and industry of the other firm(s) in the relationship.
- Both large and small firms tend to deal with contingencies in their own industry by acquisition of firms in that industry. This is particularly so if prospects for acquisitions are characterised by high profits and growth.
- Large companies ($>$ 500 employees) use contractual JVs with large firms in neighbouring industries to reduce uncertainty and cope with contingencies.
- Large firms use equity JVs with firms in industries outside manufacturing as a first step in expanding their product/ market scope.

Friedman & Berg presented two conflicting hypotheses for JV motives : (i) the knowledge acquisition model; and (ii) the market power model of JV activity.

The theory behind the knowledge acquisition model is that rather than commit themselves to long term and expensive investment in technical knowledge, firms will look for R & D JVs, which will reduce both the time lag and the risk from the levels associated with exclusively in-house R & D activity. However, Jv-ing firms face higher costs in the form of inter-firm communication costs, shared returns, and so on. Hence the parent company's rate of return will be negatively correlated with its JV activity.

Since the market power hypothesis depends on the rate of return increasing in direct proportion to JV activity, the two hypotheses necessarily conflict.

The following model was developed :

R_i = R(R&D intensity; Size; Diversification; Joint Venturing)

where R_i = Firm (i) observed rate of return.

$$R_i = b_o + b_1 \sum_{t=-2}^{0} W_t (RD/S)_{ti} + b_2 (\text{Log } S_i) + b_3(D_i) + b_4(JV)_i + e_t$$

where :

$(RD/S)_{ti}$ = R&D expenditure relative to sales in time t for firm i.

W_t = Weights from a polynomial distributed lag.

S_i = Total firm sales in dollars for firm i.

D_i = Four digit diversification index for firm i.

$(JV)_i$ = Whether (1) or not (0) firm has had a JV within the previous three years.

The expected coefficients were :

$$b_1 > 0 \; ; \; b_2 > 0 \; ; \; b_3 < 0 \; ; \; b_4 \gtrless 0.$$

If $b_4 < 0$ this backs the knowledge acquisition model, since firms pay more for quicker, less risky technical inputs ;

If $b_4 > 0$ this backs the market power model, since JVs increase the rate of return.

Their results were as follows :

TABLE 10 Friedman & Berg

Cross Sections of the Rate of Return in Chemicals (SIC 28)

Year	N Firms	b_0 Constant	b_1 Lagged (R&D/S)	b_2 Log Sales	b_3 Diversi-fication	b_4 JVs	R^2
1973	105	3.92	49.00	3.78	-0.35	-2.71	0.18
		(1.71)	(1.93)	(3.61)	(2.65)	(1.35)	
1972	75	2.94	91.78	3.54	-0.43	-2.93	0.35
		(1.03)	(3.77)	(2.93)	(3.28)	(1.64)	
1968	39	4.86	110.12	1.77	-0.21	-4.16	0.35
		(1.25)	(3.68)	(1.12)	(1.45)	(1.84)	

Source : Friedman & Berg p. 1335.

Friedman & Berg, noting that $b_4 < 0$, admitted that the coefficients for 1973 and 1972 were not very significant, and suggested that "the size of the coefficient may reflect the fact that the managers of firms that engage in JVs are more risk averse than are others."[1]

An alternative suggestion, put forward by Asch & Seneca, is that ventures may be in response to past low profitability.

"Our tentative conclusion," wrote Friedman & Berg, "is that neither theory nor descriptive/statistical evidence supports the contention that the pro-competitive impacts of new entry by JVs are outweighed by their market power effect."[2]

Having added Duncan to their ranks, Friedman & Berg extended this analysis to two types of JVs for nineteen industrial groups over a period of ten years.

Their results confirmed their findings against the market-power hypothesis, indicating that "knowledge-acquisition JVs lower rates of return relative to non-JVing firms", and that "When firms participate heavily in knowledge-acquisition JVs, the industries tend to have lower rates of return than they would otherwise."[3]

However, they also state that "other JVs increase rates of return" without giving any further details or explanations. They noted that "the expected profitability of each firm is higher (or the risk lower) than in the absence of a JV."[4]

They suggested that a case-by-case rule should be used in evaluating the competitive effects of JV activity.

Friedman, Berg & Duncan then went on to measure the extent of JV and R&D substitution by considering the level of internal R&D which was performed by JVing firms relative to the level which was performed by non-JVing firms.

---

1 Friedman & Berg, p.1336
2 Ibid, p.1331
3,4 Friedman, Berg & Duncan, p.194

The functional firm for this substitution test was :

$$R\&D = a_0 + a_1 S + a_2 S^2 + a_3 CF/S + a_4 JV$$

where

R&D = R&D expenditures for 1973
S = Sales for 1973
CF = Cash Flow for 1973
JV = 0 if no JVs formed by the firm
= 1 if a JV was formed.

The expected signs were : $a_1 > 0$; $a_2 \gtrless 0$; $a_4 < 0$.

The results were as follows :

TABLE 11

Friedman, Berg & Duncan :

R&D as a function of Sales and JV activity, 1973

	a_0	$a_1 S$	$a_2 S^2$	$a_3 CF/S$	$a_4 JV$	R^2
Chemicals	-7.59	0.0174	4.2×10^{-6}	161.4	-12.6	0.820
	(-1.41)	(2.76)	(2.90)	(3.82)	(-2.10)	
Resource Processing	-1.14	0.010	-3.6×10^{-7}	-4.68	0.055	0.786
	(-0.52)	(6.56)	(-2.32)	(-0.198)	(0.020)	
Engineering	-16.3	0.0357	1.9×10^{-6}	216.3	-14.9	0.933
	(-5.2)	(22.3)	(-0.36)	(5.77)	(-2.59)	

Source : Friedman, Berg & Duncan p.105

Thus for chemicals and engineering $a_4 < 0$ while for resource processing industries $a_4 > 0$. Since Friedman, Berg & Duncan describe chemicals and engineering as high technology industries, they claim that these results support the view that knowledge-acquisition JVs substitute for internal R&D expenditures of technologically intense firms, while the hypothesis that all industries conform to the same JV pattern is rejected.[1]

1 Ibid, p.105 The present study confirms that JVs - and also acquisitions - may be used as a substitute for internal R&D (see p 208.).

They concluded "The validity of interpreting JVs as an innovative substitute for internal R&D expenditure depends upon the specific industry that is being considered. Those industries that do not engage in such substitution tend to engage in distribution or resource risk-pooling ventures. The data indicate that those industries and firms that have relatively high R&D intensities can be presumed to be using JVs as innovative substitutes."[1]

They provided the following distribution of JV characteristics by industry :

TABLE 12

Friedman, Berg & Duncan : Percentage Distribution of JV Characteristics by Industry, 1964-74

Industry	SIC	Technology/ Knowledge	Resource Construction	Marketing
Computer	357	56.3	-	43.7
Instruments	38	61.1	-	38.9
Transport Equipment	37	82.7	13.5	3.8
Electrical Equipment	36	71.4	14.3	14.3
Chemicals	28	43.8	43.2	13.0
Non-Electrical	351	45.8	20.9	33.3
Miscellaneous Machinery	32/35	52.8	36.1	11.1
Metal/mining	10/33	30.7	60.2	9.1
Petroleum	29	25.8	65.3	8.9

Source: Friedman, Berg & Duncan, p.107

Hlavacek & Thompson went on to write more about JVs in technology intensive industries, concentrating on new product JVs. Noting the lack of previous research in this area, they stated that their work was only exploratory, and that they did not intend to "prove" or "disprove" each of their hypothese in the classical sense.

Nevertheless, they did provide the following six working hypotheses :

1) New product JVs will original mostly in firms which are technology intensive and/or have changing technologies.

1 Friedman, Berg & Duncan, p.108.

Not surprisingly supported by the results, this perhaps seems obvious - but it does not surely apply only to JVs. New products themselves will no doubt originate mostly in such firms.

2) New product JVs will most often occur between a technical contributing firm and a marketing contributing firm with the former as most often the initiator.

This was supported by the results - "in our sample, at least, a "technology push" was more prevalent than a "market pull" transfer of technology".[1]

3) The technology-contributing partner will be smaller (in yearly sales volume) than the marketing contributing partner.

This too was supported by their results.

4) When one of the contributing firms is relatively larger, the larger parent will exert more influence after the new product JV is formed (and maybe before as well).

Hlavacek & Thompson's results suggest that potential conflicts from parental size differences could be avoided with a detailed JV agreement. "It is possible that by thorough planning, incorporating the results in a detailed legal document, most problems arising from parental size differences can be avoided. Further discussions with JV managers revealed that the differences in corporate goals between large and small firms was the major problem to resolve".[2]

5) A more deliberate and analytical search, analysis and negotiation prior to forming a JV will occur when one or both of the contributing firms is large.

This was again supported by the results, but is also perhaps an obvious point. As Hlavacek & Thompson themselves admit, "five of the smaller JV partners stated that they did not have either the time or personnel to conduct such formal evaluation."[3]

1,2 Hlavacek & Thompson, p.38. See also p.p. 46, 115-116 and 194.
3 Ibid, p.39. See also the present study, p. 194.

6) The close physical proximity of the JV to either contributing parent will interfere with the rapid integration of personnel into the new JV organisation. There was some evidence to support this view.

Asch & Seneca questioned whether collusion is profitable at all. "The major finding of this paper," they wrote, "is the consistently negative and significant relationship between firm profitability and the presence of collusion. This result may indicate the inappropriateness of some common notions about the role of collusion and about the economic impact of public policies to prohibit collusion."[1]

In criticism, though, it must be said that the direction of causality is not clear - Asch & Seneca cannot say whether collusion causes low profitability of vice-versa. They admit this weakness, and suggest three possible explanations of their results :

a) Collusion may consistently lead to lower profitability (which they regard as being an unsatisfactory explanation);

b) Unsatisfactory profit performance may motivate firms to collude;

c) "It may be that.....antitrust prosecution centres largely on the unsuccessful manifestations.....Simply put, poor collusive performances are more likely to be discovered."[2]

Asch & Seneca concluded that the latter two alternatives seem the most plausible, and may in fact reinforce each other. "That is, relatively favourable profit performances may induce overt collusive agreements which then proceed under conditions that are frequently discouraging to their success."[3]

It should be noted here that Asch & Seneca's sample was made up of illegal collusions picked up by the US antitrust authorities. These were cartel arrangements rather than JVs.

Asch & Seneca suggested that successful collusions were more likely to remain undetected by the antitrust authorities,

---

1 Asch & Seneca, p.7
2 Ibid, p.8
3 Ibid.

so that their sample only represented an unrepresentative part of the total.

This explanation is, it must be said, rather weak. There is no convincing explanation of why a poor performance should be more likely to be discovered than a strong one. There is no reason why unsuccessful firms should be forced into overt agreements, while successful firms have covert agreements for which there is no evidence, since they are not picked up by the antitrust authorities. Asch & Seneca were unable to provide any evidence to support these contentions.[1]

A number of JV writers have mentioned the question of firm size. As Boyle put it: "Firms joined together to achieve some specific function, typically some form of horizontal or vertical integration, typically give as the basic reason for their 'associations' the argument that the participating firms are either technically or financially unable to engage in the desired activity alone, a line of reasoning that implicitly assumes, of course, that the parent companies are relatively small. In fact, however, such situations are rarely found. JVs themselves are typically small manufacturing companies, while the parents are more often the country's very largest firms".[2]

Pfeffer & Nowak concurred with this, finding that joint subsidiaries are frequently relatively small organisations formed by large competing or vertically related firms. While their data did not cover the size of the JVs in their sample, the median level of assets of the parents concerned was $549.5 million (in 1976). "It is difficult convincingly to argue," they wrote, "that firms of this size require JVs to achieve economies of scale. Further, it is not readily apparent why firms of this size require JVs for risk sharing.....it is hard to argue that much of the observed JV activity can

---

1 The present study seeks to resolve the question of the role of profitability by asking firms directly what part in their investment decisions was played by their own declining profitability (see pp 44, 170 and 177).

2 Boyle, p.92

be explained by the requirements for raising capital to undertake a venture."[1]

Boyle claimed that there is a positive relationship between the size of a company and its participation in JVs. He pointed out that 42% of the 100 largest manufacturing firms in the USA have had joint subsidiaries, compared to only 4% of the firms in the 401st to 500th largest size class.

Edstrom's results also showed a weighting towards larger firms in JV behaviour, as seen below:

TABLE 13

Edstrom : Classification of Strategy According to Company Size

Strategy	Size of Company Large (%)	Small (%)
Acquisitions: Acquiring firms	43	57
Acquired firms	5	95
Equity JVs	73	27
Contractual JVs	69	31

Source : Edstrom, p.488

He showed that while 95% of his acquired firms were small ($<$ 500 employees), 57% of the acquiring firms were also amsll. 73% of the equity JVs and 69% of the contractual JVs involved large firms.[2]

Reference has already been made (p.38) to Hlavacek & Thompson's results on potential conflicts from parental size differences. They found that new product JVs usually take the form of a 'technology push' by a small initiating firm with the other typically larger firm providing marketing and financial resources. They suggested that "a detailed JV agreement will protect the smaller contributing parent from the often more ambitious objectives of the larger

1 Pfeffer & Nowak, p.328. See also the present study, p 176.
2 Edstrom, p.488. His results have already been presented on pp 31-33

contributing parent" and that "by virtue of its possession of the new technology, the technology partner can hold its own regardless of size."[1]

Finally, Gullander found that the major reasons for entering JVs are as follows :

i) to satisfy nationalistic demands ;

ii) to benefit from economies of scale, crtical mass and the experience curve effect ;

iii) to decrease dependency on other firms, and

iv) to circumvent market imperfections.

In a discussion on which stragegy suits particular types of firms, Gullander considered three alternatives : a) 'Go it alone'; b) Acquisition-merger; c) Joint Venture.

He wrote: "The 'go it alone' route would be suitable for firms which have a strong worldwide competitive position based on size, a 'world-beater' product, or any other quasi-monopoly advantage in the form of technology and management, for instance.....both small single-product firms and large diversified companies benefit highly from JVs. Large single-product companies are more inclined towards acquisitions or toward going it alone. The former choice becomes more likely when concentration of the industry is heavy and the firm has financial strength."[2]

He concludes that "the JV is both a substitute for and a compiement to the merger."[3]

The question of policy alternatives will be considered in **Chapter 3, on 'Entry Strategies for E.C. Markets'.**

---

1 Hlavacek & Thompson, p.39. See also pp 115-116 and 194 on the importance of a strong written agreement.
2 Gullander (II), pp105-107. See also pp103-104 of the present study.
3 Gullander (I), p.114

8. Weaknesses of previous studies and the development of the present study.

The literature is in the main confined to US national JVs. The joint venture is studied in respect of its use as an alternative to takeovers/mergers in an environment of strong antitrust laws which often precludes the possibility of the use of the latter stragies. The present study looks at joint ventures which have been undertaken for their own sake, not as a substitute for mergers or takeovers, as well as examining takeovers in their own right.

Gullander's work comes the closest to the EEC case, in that he looks at the European industrialised countries. His studies were limited to ventures involving at least one Swedish firm, and with a few exceptions most of the firms concerned were part of large multinational groups.

The US literature is based on national JVs, and as such does not consider JVs between one firm in the market and one outside. As will be demonstrated in this study, a JV may be used by one firm previously outside the market as a means of breaking into it. Horizontal international JVs may thus be somewhat closer to vertical domestic relationships than to horizontal domestic relationships.

None of the previous studies has looked at British or intra-EEC ventures. This is a major gap in the literature. The present study is therefore devoted to looking at these types of ventures, the survey covering transnational intra-EEC ventures involving one British firm in each case.

Neither does the US literature consider the role of a culture gap in motives for JV formation. This will be shown in the present study to be one of the most important aspects of international joint venturing.[1] Almost half of the 366 JVs which were recorded by the EC Commission in 1980[2] were international operations, and the proportion had been higher in previous years. [3]

---

1 See, for example, pp 184-185 and 202-204.

2 Latest available statistics.

3 See pp. 4-6

The role of profitability in motives for JV formulation is open to question. Other writers have been unable to establish the direction of causality on whether collusion leads to low profitability or vice-versa. It is difficult, too, to determine the profitability of a JV since such operations typically form only a very small part of the parent companies' activities. Even if JV profits were presented separately (and they are generally amalgamated with other group results in the parents' accounts) they could not say much about the success of such ventures. Profit figures can be manipulated through transfer pricing techniques or the charging of management fees; increased profits may not have been the motive for a venture; a venture may not be expected to return to profitability for some years in a long term investment.

In addition, it may be difficult to detect the purpose of a JV or takeover from its post-profit performance because intentions and outcomes are not necessarily the same thing. A number of the ventures examined in this study have failed, so that the purposes of the agreement could not be detected by any analysis of their subsequent performance.

Moreover, low profitability may be one reason why firms should seek joint ventures; but it can be a very important reason why such firms will not be able to find a JV partner. Few firms are willing to commit resources to a venture with a financially weak partner, particularly when that partner is in a foreign country.[1]

The problem is resolved in the present study by asking firms directly, through the use of a questionnaire, how important a part was played by declining profits in deciding on the venture.

---

1 See pp. 39-40, 170 and 177.

Writers who claim that a joint venture is anti-competitive if it results in an increase in market power for the parent companies should also be careful. By increasing their market shares, these firms may be demonstrating a greater efficiency which their competitors have been unable to match. If this forces those competitors to strive in turn for greater efficiency, the competitive effects may indeed be positive, and not negative.

On the question of industrial concentration, published concentration figures may be misleading for two reasons :

i) they may amalgamate a number of separate markets, giving an overall average where actual concentration may vary widely;

ii) there may be high export and/or import ratios for the industry, so that concentration figures based on production shares may be meaningless as far as the domestic market is concerned.

Published statistics may therefore not represent accurately the true position which faces firms. The present survey therefore uses other methods of examining concentration.

Attempts have been made to provide a subjective estimate of concentration and strength of competition through the questionnaire. This has been done by asking firms (i) how strong industrial concentration is on a scale of 1-10 (1 being very low, and 10 being monopoly); (ii) how important competition was in a) the home market and b) the JV market in making the JV decision.[1]

By concentrating on individual ventures, it is possible to determine whether there has been an increase/decrease/no change in the number of competitors in the market concerned, and whether any restraint in competition has resulted.[2]

---

1 See pp. 166-167 and 198-202.

2 See p.200.

Some of the other factors which have been mentioned by other writers and which are also covered here are : the role of the shortage of capital; risk; complementary/overlapping technologies; the competitive relationship between the parents (horizontal, vertical, conglomerate); and firm size. The shortage of data, together with the fact that some of these operations took place some years ago, makes it impossible to examine any of the countermeasures which Backman (see p. 30) suggested might be taken by other producers in response to a JV.

Hlavacek & Thompson's point (p. 38) about the strength of the JV agreement will be taken much further. This will be shown to be a very important practical issue in international joint venturing.[1]

Other factors to be examined may relate more to Chapter 3 on corporate strategy. These include: joint venture motives (listed in order of importance); partner search; ownership and control; problem areas; and lessons learned by the firms concerned.

As far as methodology goes, most of the studies have relied on published data, with only Gullander and Hlavacek & Thompson using personal interviews with JV managers. Edstrom wrote that the use of industry data can lead to generalisations being made unjustifiably, but that data for individual firms is difficult to obtain.[2]

The weaknesses of using published data have been pointed out, however, and in spite of Edstrom's reservations on obtaining data on individual firms it is considered that only through the collection of such data is it possible to carry out an adequate analysis.[3]

The present study is therefore based on personal interviews

---

1 See pp 115-116 and 194.
2 Edstrom, p.479.
3 For the success of this method, see p158-63 on response rates.

using a detailed questionnaire.[1]

In order to avoid variations due to different industry characteristics, the present study is confined in general to the mechanical engineering industries (though one electrical engineering and two instrument engineering ventures are included). The reason for choosing mechanical engineering is that while accounting for 9% of industrial employment and 12% of output, the UK industry accounts for some 30% of UK international trade. The industry thus has a highly international flavour, as indicated by its relatively high import and export ratios (see Chapter 4, 'The Mechanical Eggineering Industry', pp 119-123). The industry also accounted for 20% of the work of the Business Co-operation Centre between 1973 and 1980.[2]

None of the other studies have been restricted to this one industry.

---

1 See Chapter 5 for details.
2 See Tables 5 & 6, pp 11-12.

CHAPTER TWO

EEC POLICY ON CO-OPERATION

The object of this chapter will be to first discuss the thinking and philosophy which lies behind EEC policy on co-operation between enterprises, and then to discuss the application of EEC legislation to specific issues.

The fundamental philosophy underlying EEC policy on co-operation is the preservation and enhancement of competition. This is seen by the EC Commission as being quite central to the economic structure of the Common Market and to improvements in both technology and the general standard of living within the Community.[1]

At first sight, co-operation between companies would appear to represent an impairment of competition through reduding the number of competitors in the market, but the two concepts are not necessarily incompatible.

The Commission wants to encourage co-operation as a means of furthering or speeding economic and technical development and in helping European firms to compete more effectively against US and Japanese multinational companies. Also, by encouraging small and medium-sized firms to co-operate it can increase competition by reducing the possibility of customer dependence on a few oligopolistic firms. In addition, commercial and industrial co-operation helps to shift the Member States towards the economic integration which is the eventual aim of the European Commission.

However, encouraging co-operation lays the Community open to market sharing agreements, domination or market foreclosure operations between the larger firms, and other anticompetitive

---

1 See Commission of the European Communities (herinafter referred to as 'the Commission'), First Report on Competition Policy, p.11, for a statement on the importance of competition.

measures. Simply limiting agreements on the basis of company size would not be an adequate answer, however, as the Commission recognises that co-operation among large enterprises can also be economically desirable without presenting difficulties from the angle of competition policy.[1]

Furthermore, such developments may well be necessary if the Commission wants to transform Community enterprises from being nationally-based into European operations.

The problem is thus achieving a balance between co-operation and anticompetitive measures.

In answer to the question on which side of the argument the Commission will descend, it has declared the ultimate and wholly essential good as being the preservation of competition. That is, no matter how great the advantages from economic and technical progress or improvements in production and distribution, a co-operation agreement may be ruled inadmissible by the Commission if it results in an impairment of competition. Whether or not the agreement will be disqualified is left, however, entirely at the discretion of the Commission. Its approach has been to place the emphasis on the economic effect of a co-operation just as much as its intention.

Since the economic advantages and competitive consequences of agreements naturally differ according to their individual circumstances, it is not possible to legislate on a broad basis beyond the guidelines presented in the rules on competition policy in the Treaty of Rome, and Commission judgements are thus made on a case by case basis.[2]

---

1 See EC Commission, 'The European Community's Competition Policy', p.6.

2 The Commission has, however, created block exemptions for agreements of minor importance (see Appendix 2 for details) and for specialisation agreements below a certain size (see Regulation 2822/71 in Appendix 2 for details).

The framework of EEC Competition Policy is contained in Article 85 and 86 of the Treaty of Rome. Collaboration between companies is covered by Article 85. Where effective competition does not exist because of the existence of a dominant position by one or more companies, prevention of the exploitation of such a position is catered for by Article 86.

The object of Article 85 is to permit collaboration, but in a controlled way.

The problem with Article 86 is that while it prevents the exploitation of a dominant position, it does not actually forbid a dominant position at all, nor the manner in which it is acquired, and thus ignores the question of why a firm should seek to acquire such a position in the first place. Once the dominant position has been attained, the competitive structure of the industry has already changed. Article 86 thus takes a static view of the competitive situation, whereas a dynamic approach would take account of market conduct which affects market structure and thus changes the competitive situation over time.[1]

The acquisition of a dominant position brings up the question of mergers and takeovers, which are not mentioned specifically in the Treaty of Rome. There is therefore a gap in the EEC Competition Policy, which the Commission hopes to fill with new legislation - namely, the proposed Merger Control Regulation, which is also discussed in this chapter.

While recognising that collaboration can result in benefits, the Commission's commitment to free and undistorted competition is such that it will not favour co-operation where the end of technical or economic progress, etc., can be achieved without a collaboration.[2]

---

1 See A.Jacquemin, p.137, for a criticism of Article 86 along these lines.

2 See Official Journal of the European Communities (hereafter referred to as 'OJ') L 30, 5.2.1976, p.19 for a statement of this commitment.

That is, it is not sufficient for a collaboration simply to result in benefits. It must constitute an improvement on the situation that would otherwise exist, not merely on the present situation.

The Commission's philosophy is that co-operation should be employed as the most effective means to an end, not as an end in itself. For this reason, it is concerned that any collaboration should not continue for longer than necessary and that the participants should afterwards be able to regain their economic independence without difficulty. Any other prospective outcome would imply co-operation for its own sake, and the Commission's view is that this would very likely lead to concerted practices in any of a number of different areas, from research and investment to marketing.

The case by case approach of the Commission to co-operation agreements means that an analysis of its attitudes can best be carried out by examining different types of agreements. This is done in part b) of this chapter, which also examines the extent to which the Commission will allow firms to agree not to compete with each other, together with any other factors, such as the market power of the joint venture's customers, which the Commission may take into account in its decision. This section is completed by a case study of the only prohibition decision so far adopted under Article 85.

Having covered the matter of co-operation, the question still remains of how to actively encourage firms to become 'European' in their attitudes. The Commission is concerned with providing the conditions necessary for this process, which introduces the subjects of company law and corporate taxation. The Commission believes that differences in corporate legal and fiscal systems are a barrier to understanding and to the transnational process in the EEC. The creation of uniform conditions will therefore encourage both firms and investors to develop a more European outlook and thus aid the creation of a single Community market. It believes that this will ensure that the widest possible choice will be available to customers and will also aid economic integration within the Community.

If in the course of becoming European in nature it will be necessary for firms to merge or form joint subsidiaries across borders, a common corporate form will be called for which can circumvent the legal, fiscal and psychological impediments. This reasoning is the basis for both the European Company and its later and simpler modification, the European Co-operation Grouping.

Where such a corporate form is not necessary, such as when firms do not wish to co-operate, companies still face problems in trying to establish a European presence because of the different fiscal and legal systems which operate in the EEC. Before a single European market can be established, then, it is first necessary to create uniformity in corporate taxation and company law. The company law directives seek uniformity in information, accounting behaviour and company structure, while proposals in the area of taxation are aimed at preventing distortions in the free movement of capital.

Harmonisation of these issues, which are discussed at greater length in part c)of this chapter, is again not an end in itself but is seen as being the means to the overall end of economic integration in the EEC.

Topics to be covered in this chapter are thus :

Part a): Competition Policy in the EEC.

- The application of Articles 85 and 86;
- The proposed Merger Control Regulation.

Part b): The EC Commission's decisions on joint ventures.

- General attitudes;
- Types of joint ventures;
- Other considerations;
- Case study; ICI-Wasagchemie, 1978.

Part c): The Company in Europe.

- The European Company;
- The European Co-operation Grouping;
- Harmonisation of Company Law;
- Harmonisation of Corporate Taxation.

Part a): Competition Policy in the EEC

- The application of Articles 85 and 86.[1]

i) Article 85

Article 85 is designed to eliminate agreements which have the object of effect of preventing, restricting or distorting competition within the EEC, and are liable to affect trade between Member States. To qualify for exemption, an agreement must result in an improvement on the situation that would otherwise exist. That is, it must :

a) help to improve the production or distribution of goods; or
b) promote technical or economic progress;
c) allow consumers a fair share of the resulting profit;
d) not result in any restrictions on the firms involved which are not indispensable to the attainment of the agreement's objectives; and
e) not result in an elimination of competition in respect of a substantial part of the goods concerned.

The Commission may prohibit an offending agreement, in which case it is automatically void, it may exempt it from the prohibition under clause 85(3), or it may grant the agreement a 'negative clearance' by stating that the facts available to it reveal no need for action.[2]

It is helpful to distinguish here between horizontal and vertical agreements. Horizontal agreements are those concluded between companies at the same stage of the industrial or commercial process. Joint sales/purchase organisations or cartels are examples. Since the companies concerned are involved in the same product market, and are at least potential competitors in the same geographic markets, there may be a significant chance of a restriction of competition.[3]

---

1 Articles 85 and 86 are reproduced in full in Appendix 2.
2 The regulations implementing Articles 85 and 86 are contained in Regulation No. 17 of the Council of 6.2.1962, OJ 13, 21.2.1962, p.204.
3 See J. Temple Lang, p.31, for a development of this argument.

Although a horizontal cartel would only be permitted by the Commission if its market share were unimportant, or if it were a common sales/purchase organisation operating outside the EEC only, contractual restrictions on competition between a joint venture and its parents may be permitted if it does not infringe upon competition which would exist without the formation of the JV. On the other hand, Article 85(1) would apply if the parents required the JV to perform activites with respect to which they were formerly actually or potentially competing. This holds whether the restriction is by agreement or by effect. [1]

Vertical agreements are those concluded between firms in successive stages of the industrial or commercial process. An example is an agreement between a manufacturer and an agent or distributor.[2]

While exclusive dealing contracts[3] may well fall within Article 85(1),[4] exclusive agency agreements do not. This is because the party which appoints the agent is free to decide the product and/or geographic market within which the agent should operate. In the same way, in the case of Christiani & Nielsen (1969),[5] the Commission decided that the imposition of marketing restrictions by a parent company on its wholly-owned subsidiary could only be considered as a division of tasks within the economic organisation of the group as a whole. As Mathijsen has pointed out, "where there is no economic autonomy there can be no competition and therefore no restriction of competition."[6]

---

1 See H-G Koppensteiner, p.308, on this point.
2 For a description of these strategies see Chapter 3, pp 84-86.
3 de Jong notes (pp 43-44) that exclusive dealing is only objectionable if agreements between independent trading partners contain export prohibitions to other areas.
4 As stated by the Commission in OJ 139, 24.12.1962 p.2921.
5 OJ L 165, 5.7.1969, p.12
6 P.S.R.F. Mathijsen, pp.80-81.

The Commission regards the decisive criterion which distinguishes the commercial agent from the independent trader as being whether the agent assumes the risk arising from the transactions. If he does so, his function becomes akin to that of an independent trader.[1] An example of an illegal exclusive distributorship - by which a producer attempted to maintain a price differential between two countries by preventing a distributor from re-selling in the more expensive market - was provided by the Commission's decision to prohibit the Grundig-Consten agreement.[2]

In case of a licensing agreement,[3] restraints on the licensee can only fall under Article 85(1) to the extent that they are not covered by the legal scope of the protective right under licence. On the other hand, restraints on the licensor cannot come under the protective scope of the licensed right, since that scope includes only prohibitive rights on the part of the owner, and may therefore come under Article 85(1).[4]

ii) Article 86

The Commission's definition of a dominant position is when an enterprise has the power to behave independently without taking into account, to any substantial effect, its competitors, purchasers and suppliers.[5]

In order to be able to assess the extent of an enterprise's power, the Commission needs to know such factors as: the firm's market share; the competitive structure of the industry; the firm's product range; the extent of its technological leadership; the ability of new firms to enter the market; the existence of substitutes; and the market power of the customers.[6]

---

1 OJ 139, 24.12.1962, p.2921.
2 OJ 161, 20.10.1964.
3 Competition rules on licensing agreements are contained in the 'Notice on Patent Licensing Agreements,' OJ 139, 24.12.1962, p.2922. A description of this strategy is given in Chapter 3, pp 89-92.
4 This point is followed up by Oberdorfer et al., p.59, who along with Bellamy & Child give an extensive treatment of Articles 85 and 86.
5 This was established in the Continental Can case, OJ C 68, 21.9.1973, p.33.
6 See Open University, pp.39-40, for a further analysis of these indicators.

The Commission's policy on the application of Article 86 to takeovers is that the acquisition of a competitor by a dominant firm, with the result that only undertakings remain in the market which are dependent on the dominant firm and which do not constitute an adequate counterweight, amounts to an abusive exploitation of dominance.[1]

- The proposed Merger Control Regulation.

While Article 86 may thus apply post hoc to concentrations which result from a strengthening of market dominance and which substantially impair competition, the Commission wishes to strengthen this policy through a regulation which would assess mergers and takeovers[2] prior to their being carried out, regardless of whether they arise from a previously existing dominance of one of the enterprises concerned. This is the basis for the proposed Merger Control Regulation.

This draft regulation, issued in 1973[3], sought to prohibit any merger by which a firm could acquire or enhance the power to hinder effective competition in a substantial part of the Common Market. Firms below a certain size would be exempted. The Commission suggested in its amended proposal that this limit should be drawn at 20% of the turnover of the product concerned and its substitutes in the Common Market, and at an aggregate turnover of the undertakings concerned of 500 million EUA. The Economic and Social Committee of the Council of the EEC accepted the proposal,[4] subject to the proviso that the Commission should not see planned mergers in black and white terms just because of the market share criterion. The Committee also proposed that the turnover limit should be fixed at 350 million EUA, with a periodic review.

---

1 Stated in EC Commission, Third Report on Competition Policy, para.1, and confirmed by the Court of Justice in the Continental Can case, OJ C 68, 21.9.1973, p.33.

2 A description of this strategy is given in Chapter 3, pp.92-98.

3 Original proposal : OJ C 92, 31.10.1973, p.1. Amended proposal : OJ C 36, 12.2.1982, p.3.

4 Opinion of the Economic and Social Committee, OJ C 252, 27.9.1982 p.16.

The Commission believes that this regulation would give it the means to take effective action at Community level against any irreversible structural evolution which could seriously jeopardise competition. For this reason the European Parliament, in its Resolution on the Ninth Report on Competition Policy[1] expressed considerable disquiet that the Council had still not adopted the regulation, sentiments which have since been echoed by the Economic and Social Committee.[2] The reason for the delay by the Council is that its discussions on the subject have revealed significant differences of opinion, relating mainly to the scope of the regulation and to the division of decision-making power between the Commission and the Council.

Despite the proposed regulation, the Commission does not believe that enterprise concentration is per se necessarily a bad thing; indeed, it has believed for many years that concentration could achieve rationalisation benefits and economies of scale, and thus help to counter competition from large US and Japanese multinational corporations.[3] Moreover, it is possible that acquisition as a means of market entry by a firm outside the market may disturb the status quo in the market and, if it results in a struggle for market shares, may result in a rejuvenation of competition.[4]

---

1 OJ C 144, 15.6.1981.
2 OJ C 252, 27.9.1982, p.15
3 See 'Effective competition between oligopolistic enterprises is in keeping with the Treaty objectives', 1965 Commission Memorandum to Governments of Member States on Concentration of Enterprises in the Common Market.
4. This point is developed by J-F. Bellis, p.25. See also the present study, p. 200.

Part b): The EC Commission's Decisions on Joint Ventures

- General attitudes.

The definition of a joint venture (JV) used by the Commission is : an enterprise subject to joint control by two or more undertakings which are economically independent of each other.[1] The weakness of this definition is that it does not cover the 'contractual' JV,[2] which does not take a corporate form. A better definition would be that a joint venture is a collaboration between two or more firms in one or more areas of activity.[3]

However, the Commission's definition is flexible. In the case of GEC-Weir Group (1977)[4] the co-operation was purely contractual, although the arrangement had all the most essential characteristics of a JV in that it provided for joint control by the two firms of all the activities relating to the product concerned, including planning, financing, research, development, manufacture and sale. The Commission saw no distinction between a case of this sort and its normal definition of a JV, which requires a new company.

The policy is that exemption under Article 85(3) should be refused wherever the formation of a JV does not offer substantial economic benefirs and wherever there is a chance that competition on the relevant market may be appreciably reduced. Co-operation between large firms in different Member States which have either the object or the effect of co-ordinating their market activity will thus generally meet with an unfavourable Commission reaction, as will any JV whose benefits could be achieved by less restrictive means. The Commission will, however, consider whether competitive

---

1 Fourth Report on Competition Policy, point 37.
2 See p.15.
3 This definition was first suggested by V.Korah, p.136. For other definitions see pp. 15-16.
4 OJ L 327,20.12.1977, p.26.

restrictions could be minimised by a watered-down agreement including the imposition of obligations and conditions on the partners before refusing exemption for a JV.[1]

This point was illustrated by the decision on the Bayer/Gist-Brocades agreement of 1975,[2] where a joint venture was not regarded as indispensable, although a specialisation agreement was permitted.

Two years previously, the Commission had described cases in which problems can arise as generally being those in which JVs operate as genuine economic entities for the purpose of producing or distributing goods or services, with the likely effect of inducing the controlling undertakings to adopt a policy of mutual non-competition by means of the actual creation or management of a JV.[3] This involves a partial integration of the parent companies. In order to assess its significance, the Commission has to consider the importance of the parents, the spread of their activites and the relative size of the JV within this, market structures, and the possible effect on the interaction between the parents in other markets. Again, this necessitates a case by case approach.[4]

The Commission has stated that in heavy industries, in which investment expenditure is considerable, the joint formation of a major production unit may qualify for exemption if the new joint production capacity remains below the capacity of each of the parents and as long as the parents retain independence with respect to the marketing of the joint product.[5]

---

1 Sixth Report on Competition Policy, point 59.
2 OJ L 30, 5.2.1976, p.13
3 Fourth Report on Competition Policy, point 37.
4 See Fourth Report on Competition Policy, point 41.
5 The Commission bases this view on its experience in cases under Article 66 of the ECSC (European Coal and Steel Community) Treaty - see Fourth Report on Competition Policy, point 42.

Where the Commission does make an exemption, its duration is not uniform, but depends on the particular circumstances of the case. The Commission may confine its authorisation to a relatively brief period (between five and ten years) in order to stress the provisional nature of the co-operation in a JV. This would apply where the JV is formed to enable one of the participants to enter production more quickly by having access to the knowhow and experience of the other. It could also apply in the development or manufacture of new products where serious technical difficulties or financial risks are encountered, necessitating co-operation between two or more firms for a transitional period, as in the case of Vacuum Interrupters.[1] On the other hand, it may be that the objectives of co-operation could only be achieved in the long term, and exemption would be pointless unless it were granted for a relatively long term.[2] In the KEWA case (nulear fuels reprocessing), the Commission fixed this period at fifteen years.[3] In any event, on termination of the venture both parents must be free to benefit independently from the results of the co-operation.

There are conflicting views on a 50/50 ownership structure in a JV. One view is that such a structure can yield important feelings of co-operation and equality, regardless of the respective sizes of the parent companies.[4] The Commission sometimes sees it rather differently. In the cases of ICI-Wasagchemie (1978)[5], which was eventually prohibited - though not for that reason - and GEC/Weir Group (1977)[6], the Commission feared that joint control of the JV would mean that neither parent would be able to make independent business decisions on any matter of importance relating to the product. The effect of the JV and of the agreement would be to change each party's position of autonomy in this respect to one of joint activity concerning planning, financing, research, development and sale, with each party abandoning its individual freedom of action in relation to these activities. This may affect not only the

---

1 OJ L 48, 19.2.1977, p.32.
2 Sixth Report on Competition Policy, point 59.
3 OJ L 51, 26.2.1976, p.15.
4 See, for example, Gullander (1), p.110. See also pp 217-218 on the results of the present study.
5 OJ L 322, 16.11.1978, p.26.
6 OJ L 327, 20.12.1977, p.26

running of the JV itself, but also the parents' own activities in the same field.

The Commission has thus sometimes seemed to fear that the power of veto in a 50/50 JV[1] could prove to be a restriction of competition. However, in the event of such a veto being used, the breach of trust and lack of confidence which inspired it would in any case mean that the joint venture may well have been doomed to failure in the first place. Nevertheless, the joint management and control of the JV by the parents does mean that the activites mentioned above can become group, rather than company, policies. In fact, agreements which cause the limitation or control of production, markets, technical development or investment are specifically mentioned in Article 85 (1b) as examples of restrictions on competition.

- Types of joint ventures.

In order to avoid the dangers of excessive generalisation, this chapter now considers the Commission's attitudes to co-operation at different stages of the industrial/commercial process. The types of joint venture considered here are :

1. Research and development;
2. Investment;
3. Production;
4. Specialisation agreements;
5. Sales and purchase organisations.

1. Research and Development

The Commission's policy here is that joint research agreements do not generally restrict competition on condition that the parents are not restricted in respect of their own research activities, and that the results of the research are made available to all participants in proportion to their participation.[2]

---

1 See also pp. 112-113.
2 See the Commission's 1968 Notice on Co-operation between Enterprises' in Appendix.

In one case,[1] the oligopolistic structure of the market concerned and the great technical homogeneity of the products therein, together with high entry barriers, meant that the market position of firms and their opportunities for growth were largely determined by the degree of technical progress and innovation. The Commission consequently adjudged that competition in the field of research was extremely important, and that the prohibition of Article 85(1) could apply to an agreement between two of the largest firms.

All joint R & D is likely to meet one of the conditions for exemption,[2] namely that of promoting technical or economic progress. However, the benefits of research to consumers are virtually impossible to guage accurately, since they will accrue from future discoveries. The Commission thus often required periodic progress reports, and reports on extensions of the research, as conditions for exemption.

Freedom of the parties to maintain individual research is a standard condition for exemption. The Commission is not keen on co-operation in R & D being extended to production and marketing; it feels that such co-operation will inevitably lead to joint planning and pricing policies.

Where a product is developed from the research, its exclusive production by the JV is only regarded as an indispensable condition if it is limited to an initial period sufficient to launch the product successfully. Such a condition was allowed in the De Laval-Stork JV,[3] which gave the American company time to penetrate the EEC market.

---

1 The first Henkel-Colgate decision (1971), OJ L 14, 18.1.1972, p.14.
2 See p.53.
3 OJ L 215, 23.8.1977, p.11

An interesting point is the change of attitude shown by the Commission to the issue of licences to third parties in the Henkel-Colgate case, between 1971 and 1978. In 1971 the Commission took the view that an agreement not to allow licences to third parties except by mutual agreement of the joint venture partners was not restrictive, but was the normal consequence of a research agreement.[1] But by 1978 the Commission's view was that such a restriction on the issue of licences would mean that the parties were not free to use the results of their research independently; and that in an oligopolistic market surrounded by high entry barriers it would make it unreasonably difficult for third parties to penetrate the market.[2] The agreement was, as a result, terminated in May 1978 before the Commission had time to adopt a decision on it.

Another interesting case is that of Beecham-Parke Davis, where provisions which would have extended the scope of the co-operation from joint research and development in pharmaceuticals to cover the marketing of the products manufactured by each partner had to be deleted at the Commission's request.[3] Although an agreement was permitted, it is doubtful whether a JV (which was not applied for) would have been regarded as indispensable to the co-operation.

The KEWA agreement[4] was, however, permitted since it was designed to enable the four German firms concerned to proceed as rapidly as possible to the industrial stage of nuclear oxide fuel reprocessing by enabling them to pool their activites in research and development and to transfer technology between them in a new industry, which is of such a king that isolated effort from one firm alone is ineffective.

---

1 See First Report on Competition Policy, point 33.
2 See Eighth Report on Competition Policy, point 90.
3 Ibid, point 94.
4 OJ L 51, 26.2.1976, p.15.

The Vacuum Interrupters JV enabled two firms which would otherwise have had to invest a large amount of risk capital to spread that risk at a lower cost to each and to combine their technical skills in a highly specialised field. The Commission noted[1] that the agreement would enable the vacuum-type interrupter to be developed, manufactured and sold to consumers within the EEC on a competitive basis with those available for import from the United States and Japan. Moreover, consumer benefits were derived from the facts that durable, efficient interrupters would become available at a reasonable price and that models capable of handling higher voltages would be developed in time.

The Commission has taken a favourable stance on the joint formation of new business units that will enable the participants either to penetrate new geographic markets or to overcome the technical difficulties and face the major financial risks linked with the development of advanced-technology products, or to place the manufacture of intermediate products used by the parent companies on a profitable footing.[2] This approach was taken in the De Laval-Stork, GEC-Weir Group and ICI-Montedison joint ventures.

It believes that development joint ventures can have definite advantages over less formal agreements, with JVs resulting in: a closer sharing between the parties of all their complementary skills and facilities than would, for example, a cross-licensing and disclosure of information agreement; each party gaining a greater experience of and insight into the work of the other than would be possible through a specialisation agreement, better interaction between the parties in relation to problems; improved and more rapidly achieved technical solutions; and consequent lower levels of funding required by the parties and hence by their customers.[3]

---

1 OJ L 48, 19.2.1977, p.32.
2 See Seventh Report on Competition Policy, point 150.
3 See GEC-Weir Group judgement, OJ L 327, 20.12.1977, pp. 33-34.

2. Co-ordination of Investment

Co-ordination of investment is likely to mean co-ordination of production. Such collaboration in setting output levels for the industry will, if it affects trade between Member States, fall within Article 85(1).

United Reprocessors (URG), however, a JV for reprocessing nuclear fuels, was held to meet the conditions of Article 85(3) because of the particular economic context which included the public interest of three Member States. The primary object of this agreement is to co-ordinate investments relating to the reprocessing of nuclear oxide fuels, and each party undertakes to refrain from making any investment outside the programme. Other objects are the fixing of prices and allocation of work between plants.

The Commission believed that unless a co-ordinated approach was made in this case, the European reprocessing industry would become structured on the basis of national rather than Community requirements. It therefore held that the co-ordination of investment was an indispensable condition of the agreement. It would mean that uneconomic plants would not be set up and would enable the parties to wait until market conditions were most favourable before setting up high-capacity plants. This would reduce costs considerably because of the sunstantial scale effect in this industry; give the project the chance to benefit from the very latest technical progress; and improve customer service by raising safety standards and by stabilising irradiated fuels reprocessing services.[1] Even so, exemption was only granted for a transitional period sufficient for the industry to achieve conditions of effective competition.

---

1 Full details of the decision may be found in OJ L 51, 26.2.1976.

3. Production.

It has been claimed that production JVs are often formed to overcome urgent problems in the short - to medium-term and are not intended to last longer than necessary; and that for this reason many such agreements have been dissolved, rather than abandoned as a result of conflict between the parents.[1]

The proposed ICI-Montedison JV of 1977 laid its claim to exemption on the important economies of scale which would have resulted from their joint investment.[2] If the two firms had each built a factory for the production of aniline for their own use, they would each have been left with substantial excess capacity at the cost of a very heavy investment. But a factory between them would have just met their joint requirements, with a substantial saving resulting to both companies. Thus, although Montedison, which did not at the time possess the necessary technology, could have obtained that expertise and was therefore a potential competitor for the product in question, the Commission was willing to grant an exemption in this case. The principal reason why it was willing to do this was that on the termination of the agreement, Montedison would have been able to use its newly-acquired knowledge to become an independent competitor.[3] However, the Commission was against the JV selling the product itself, which would have enabled the parent companies to concert their sales practices. Unfortunately, the story did not have a happy ending as far as the two firms were concerned. Under heavy pressure from environmentalists, the joint venture never got off the ground and was finally abandoned.[4]

---

1 See L.Ritter & C.Overbury, p.630
2 See also pp19-20, and also p.99.
3 See Seventh Report on Competition Policy, points 156-159.
4 The venture was abandoned before the Commission could take a formal decision.

The De-Laval-Stork JV[1] was permitted for the same principal reason. In this case, the eventual termination of the JV agreement was to leave the American company, De Laval, able to compete effectively within the Common Market.

As with other types of venture, the Commission does not want co-operation in production to spill over into other areas, but prefers the participants to remain as independent as possible. If the co-operation were to extend to marketing, this would influence the marketing policies of the parents. In addition, restrictions should not be imposed on the participants with respect to output shares and purchases from the JV. It is essential that they are afterwards able to benefit independently from the JV, and that the JV must not continue for longer than is economically justifiable. This condition was imposed in the URG case and would also have applied to ICI-Montedison.[2]

4. **Specialisation** agreements

Specialisation agreements normally involve each party sacrificing part of its production but remaining free in respect of output and investment in its own specialised field. The partners can thus use each other's sales and distribution networks, and through concentrating on one product each can take advantage of economies of scale. It has been claimed that frequently, the only competition **restricted us the possibility of each firm extending production (into the other's range[3]). However, if one or more JVs are formed in order to produce or market the specialised goods, this will bring into co-ordination the parties' policies with regard to these functions in respect of all the production involved.**

Specialisation agreements are essentially agreements not to compete in a range of products, but to concentrate production and cross-supply each other. They are covered by a Commission

---

1 OJ L 215, 23.8.1977.
2 For a further discussion of these conditions for exemption see Ritter & Overbury, pp. 632-633.
3 See Korah, p.80

block exemption up to a certain size only.[1]

In the earlier versions of the Bayer-Gist Brocades agreement there was no provision for separate action on the market independently of the specialisation arrangements. Originally the plants were to be transferred to joint subsidiaries in which both firms were to hold shares and appoint directors. The formation of these joint subsidiaries would have had the effect of bringing production and investment under joint control; moreover, since each firm was to be equally represented, both in the management of the subsidiaries and on the associated co-ordinating committee, either would have been able to veto any management decision with which it did not agree. The result would inevitably have been that output would have been determined by joint agreement; neither firm would have been able to increase its production to compete against the other. The Commission could not regard such an extensive competitive restriction on investment and production as indispensable to the specialisation agreement. While the agreement itself was permitted, then, the JV was not.

5. Joint sales and purchase organisations.

The Commission made it know officially in 1968[2] that the establishment of a joint export service does not in itself conflict with the objectives of the EEC Treaty where the service acts merely as a joint market prospection agency and does not constitute an intermediate stage in distribution.

Policy in this area is rather clear-cut. If the members of an organisation account for a substantial part of the Community market, the organisation may remain responsible for marketing on

---

1 See Regulations 2821/71 and 2822/71 in Appendix 2.
2 Case of Alliance de Contructeurs Francaise de Machines-Outils, OJ L 201, 12.8.1968.

the respective domestic markets (if no exclusive brand/standard labels are involved) and on export markets outside the EEC. On the other hand, exports to Common Market countries must remain the responsibility of the individual members (the manufacturers and their dealers).

The principal aim pursued here by the Commission, particularly in the fertilisers sector, where such agreements have been common, and where in the past there had been little trade between Common Market countries, is to remove the obstacles which restrictive agreements linking large firms are liable to place in the way of the formation of a real single market between the Member States.[1]

Another decision in 1968[2] held that the provision of Article 85(1) are applicable to agreements between purchasers in the same way as they apply to those concluded between sellers.

- Other considerations.

i) Non-Competition clauses.

This concerns agreements by firms not to compete with each other. Such clauses may be allowed by the Commission if they are subject to either party's freedom to act independently where a potential customer declines to contract with the JV or where the other party declines to support the JV in the acceptance of a particular order. These conditions applied in the GEC-Weir Group and Vacuum Interrupters cases.

In the Commission's first JV decision[3], in 1974, one type of non-competition clause was allowed while another was not.

By the first, Chevron and SHV had each agreed not to compete without the prior consent of the other regarding distribution of the (petroleum) products covered by the agreement. This clause provided SHV with the assurance that the assets transferred by it to the joint

---

1 See Second General Report of the European Communities, 1968, p.47
2 Case of SOCEMAS, OJ L 276, 14.11.1968.
3 SHV - Chevron, OJ L 38, 12.2.1975, p.14

subsidiaries would not lose value as a result of competition by Chevron with those subsidiaries. The Commission held that this clause could not be said to involve an appreciable restriction of competition in view of the fact that Chevron had no industrial or commercial interest which could imaginably lead it to compete with its 50%-owned subsidiaries, and given also that SHV would disappear as an independent wholesaler on the petroleum product market, with no likelihood of ever returning.

Where a non-competition clause agreed by parent companies does not concern a JV's area of activity, however, it is generally to be considered a restriction of competition within the meaning of Article 85(1), whether the JV is regarded as a restrictive agreement or as a merger.[1] SHV and Chevron had included a clause whereby they agreed not to compete in respect of petroleum products not distributed by their joint subsidiaries. After objections were voiced by the Commission, the companies deleted this clause from their co-operation agreement.

In an earlier case[2], a non-competition clause was permitted because the parties to the agreement represented only a relatively insignificant part of the Community market; in addition, the situation on the relevant market (machine tools) did not seem likely to warrant, in the near future, efforts to diversify the range of machines produced, but was in fact tending to encourage specialisation.[3]

---

1 Sixth Report on Competition Policy, point 61.

2 Alliance de Contructeurs Francais de Machine-Outils, OJ L 201, 12.8.1968.

3 See Bulletin of the European Communities, 9/10 (1968), Chapter II, sec. 5.

ii) Market power of the JV's customers.

The Commission accepts that restrictive effects are limited if the JV's customers are powerful. The GEC-Weir Group JV's two customers were able to negotiate from a position of strength because they were in fact the only customers. In fact they actually encouraged the co-operation of the parties in the development of sodium circulators through a JV. They thus knowingly and deliberately gave up the benefits to them of competition for the compensating advantage of a composite technical solution from the JV to which the parties contributed their separate but complementary specialised expertise. The Commission took account of this in authorising the agreement.[1]

iii) JV employees.

A further problem from the angle of competition can arise over the JV personnel. This can occur when senior employees of both parties are seconded to the JV, but remain on the original party's payroll and under its administrative control. These employees may well retain interests in their employers' activities outside the field of the JV. So through their continuing association with each other within the JV, the coincidence of interests of the parties in other areas can perhaps be expected to lead to an impairment of competition between them also in these other areas. This question was raised in the GEC-Weir Group case, but was not considered serious enough to refuse the JV exemption under Article 85(3).

---

1 OJ L 327, 20.12.1977, p.33

- Case study : ICI Wasagchemie, 1978.

This case study is included here because it was the first prohibition decision adopted by the Commission under Article 85, and could also have involved Article 86. It concerns a JV between a subsidiary of Imperial Chemical Industries Ltd (ICI) and members of the Wasagchemie GmbH group (WASAG) for the manufacture and sale of blackpowder, a lowpower explosive.[1]

At the time, ICI, which no longer had its own production facilities for blackpowder, had a 100% or near 100% share of the sale of blackpowder in the UK, WASAG produced blackpowder and had around 50% of the sales in the Federal Republic of Germany.[2] Both parties had separate interests in other explosives, and were natural competitors in each other's national home markets, and indeed throughout the EEC, in safety fuse, an important downstream product of blackpowder.

Under the agreement, the JV would have appointed ICI and WASAG to be its sole distributors in the UK and West Germany respectively, and would have controlled the production for not less than 58% of the sales of blackpowder in the Community. Pursuant to the JV arrangements, ICI would (in view of its UK monopoly) have purchased blackpowder for substantially the entire UK demand only from the production of the JV and would not have been free to procure blackpowder for resale on the best terms from time to time available from other sources. Presumably the company was not concerned about this limitation.

In view of ICI's control of distribution and transport facilities for explosives in the UK, the effect would have been to block the blackpowder market in the UK to other

---

1 WANO Schwarzpulver, OJ L 322, 16.11.1978, p.26. See also the Eighth Report on Competition Policy, points 134-136.

2 Market information recorded in the Commision's Decision.

producers in the EEC, for example in France and Italy, who already had substantial overcapacities.

The Commission could not accept the companies' submission that a pooling of resources and technology would have enabled manufacture on a scale to bring about developments since manufacturing methods in the industry had remained essentially the same for centuries. Neither could it accept an application on the basis of security of supplies to the UK in circumstances of considerably under-used production capacities in the blackpowder industry as a whole. The overriding reason why the Commission could not grant an exemption was that competition for supply to the UK would have been ruled out if ICI had participated in the JV.

The matter went further than this, however. The Commission believed that the two companies intended to use this collaboration to enlarge their common interests in other areas, specifically that of safety fuse. In this market, ICI was the only manufacturer and supplier in the UK and WASAG the only manufacturer in West Germany, and the two could again have been regarded as natural competitors in both each other's home markets and throughout the EEC. Together they accounted for two-thirds of the Community's safety fuse production. Not only would this have given them opportunities and strong inducements for co-operation in aligning their prices and in the sharing of markets for safety fuse, but they would also jointly control the quantities and prices of any blackpowder to be sold by the JV for safety fuse production by any third-party competitors.

The Commission therefore warned the two companies that implementation of the JV agreement could additionally have amounted to an abuse of ICI's dominant position in the UK blackpowder market, which would have constituted an infringement of Article 86.

Following receipt of the Commission's objections, the parties informed the Commission that they no longer intended to go ahead with the JV agreement; but the Commission decided that the matter was important enough to adopt a Decision anyway, in order to establish the ground rules more clearly. Usually, however, no decision is taken after an agreement has been abandoned.

Part c): The Company in Europe

Moves towards the creation of a single European identity can take two forms within this sphere.

One approach is to create uniform legal and fiscal conditions across the EEC in order to encourage firms to cross their national boundaries, given confidence by the existence of consistent laws. The other approach, accepting that the first is an ambitious programme which is unlikely to be fully achieved in the short term, aims at providing companies with a corporate structure which can be used as a vehicle for co-operation. The Commission's belief is that this will facilitate a rationalisation of industry on a European, rather than national, basis through enabling firms to merge and co-operate across national boundaries without difficulty. In addition, it would result in access for such firms to all the capital markets of Europe, making such markets more competitive, and encourage transnational investment in Europe.

Two forms of common corporate structure are under consideration - the European Company and the European Co-operation Grouping.

- The European Company.[2]

The Commission believes that industrial reorganisation at a national level might tend to fragment markets and so constitute

---

1 See D.Thompson, pp.20-21, for a more detailed discussion in favour of a common European corporate form.

2 See 'Proposal for a Council Regulation establishing a European Company Statute', EC Bulletin Supplement 8/70 and OJ C 124, 10.10.1970.

an impediment to economic integration,[1] but has acknowledged that the establishment of European undertakings meets with legal, financial and psychological difficulties.[2] The object of the European Company is thus to provide a common corporate form, subject to a consistent constitution, which will permit companies in different Member States to merge, form a joint holding company or form joint subsidiaries.[3]

The original proposal for the European Company was made in 1959,[4] but there is as yet no sign of its adoption. The reason for this failure has been disagreement in the Council over certain aspects of the constitution, in particular on the matter of worker participation on the company board.

The argument centres around the proposed dual board structure, which has a Management Board administering the company's affairs under the supervision of a Supervisory Board by whom it is appointed. This latter board would consist of representatives of both employees and shareholders, together with members representing general interests and independent of the other two parties, although elected by them. This board structure is the same as that proposed in the Fifth Directive on Company Law. The degree of worker participation has been unacceptable to Member States in which such a structure is unknown, and the European Company will thus not come into being in its present form until the Fifth Directive is accepted.

Although subject to uniform rules regarding the presentation of accounts, it would be necessary for national taxation levels to apply to the European Company until corporate taxation rates are common throughout the EEC.

---

1 Commission, 'Statute for European Companies : Amended proposal for a regulation', p.11.

2 Ibid. It should be noted, however, that the inability to form European mergers was found to be an insignificant motive for collaboration in the present study (see p. 177).

3 See European Parliament Secretariat, para 2.33.

4 See A.J.Easson (1980, p.187n) for a note on the origins of the idea.

Otherwise, companies will only adopt such a corporate form if it results in a lighter tax burden. Furthermore, the formulation of a fiscal system solely for the European Company may result in a decrease in national tax revenue. Member States are unlikely to agree to this.

If harmonisation of company law and taxation were achieved, of course, there would be no need for the European Company.

- The European Co-operation Grouping.

With the European Company running into problems, the Commission is attempting to introduce other legislation to help small and medium sized enterprises (SMEs) co-operate across national boundaries in order to maximise their competitive impact on European industry. It believes that such firms have a key part to play by virtue of the innovative potential and employment opporunities they offer, but that they find it more difficult to establish transnational co-operations than larger firms. The Commission is concerned that this situation exists at a time when the greater sensitivity of SMEs to the uncertainties of the economic climate require, on the contrary, that operations of this kind should be made easier.[1]

The current fact that SMEs co-operating across borders have to choose a specific (i.e., national) legal structure places one partner on unfamiliar ground. The purpose of the ECG is thus to create an instrument common to all Member States which is easy to use and which can transcend the problem of national legislation. The Business Co-operation Centre (the arm of the Commission which actively promotes co-operation between SMEs) believes that the psychological importance of using this Statute will often be decisive for SMEs.[2]

---

1 These opinions were published in an informal introductory note concerning the amended Proposal for a Council Regulation establishing a European Co-operation Grouping, 23.10.1981.

2 Sixth and Seventh Progress Reports of the Business Co-operation Centre (1978 & 1979), COM(80) 448 final, 24 July 1980, p.9.

The ECG, which may not have more than 500 employees and is thus limited to SMEs, is not a separate economic entity and may not exercise management functions in respect of the business of its members. It does not aim, therefore, to make a profit for itself but only to facilitate or develop the business of its members by: a) providing services exclusively to its members; or b) producing, processing or packaging goods exclusively for its members. Its legal structure gives its members considerable freedom of action over foundation, operation and winding up.

Originally proposed by the Commission in 1973[1] and modified in 1978[2] following favourable opinions from the Economic and Social Committee in 1975[3] and by the European Parliament in 1977[4], the ECG has not yet been adopted due to delays in discussion by the Council. However, the Commission believes that a majority of delegations to the Council's Group on economic questions are favourable to the establishment of the ECG, and the concept is now under active consideration.[5]

- Harmonisation of Company Law.

The Company Law directives have, in general, the purpose of promoting the functioning of a European capital market by co-ordinating rules for public limited companies on the presentation of accounts, disclosure of information, and capitalisation requirements. They aim to protect shareholders and creditors and, through making this information broadly consistent and comparable, to help the cause of transnational investment in the EEC.

---

1 Bulletin of the European Communities, Supplement 1/74, 1974.
2 OJ C 103, 28.4.1978.
3 OJ C 108, 15.5.1975.
4 OJ C 163, 11.7.1977.
5 'Progress Report of the Commission to the European Parliament on the activities of the Commission with regard to small and medium-sized enterprises within the Community', SEC (82) 1347, Brussels, 3rd August 1982, p.16.

Directives which had been passed by the Council by the end of 1982 were: the first,[1] which deals with the disclosure of information and requirements for the publication of accounts; the second,[2] which concerns capitalisation requirements and the payment of dividends; the third,[3] which covers national (but not transnational) merger legislation and requires approval for a merger of the shareholders of both companies,[4] the fourth,[5] on the co-ordination of the presentation and content of annual reports and accounts; information to be made available to the public; and the requirement of accounts to be audited; and the sixth,[6] concerning the co-ordination of information to be provided by companies in order to obtain a Stock Exchange listing, and the setting up of competent authorities in each Member State to check this information.

Three other proposed directives have not yet been passed:

The proposed fifth directive[7] is somewhat different to the others in that it seeks employee representation, not merely in a consultative capacity, on the supervisory bodies of public limited companies.[8] This proposal has caused considerable controversy, and the issue is still a long way from being settled.

The purpose of the proposed seventh directive[9] is to institute a system of Community legislation on consolidated accounts. Arguing that the group accounts of large companies cannot by themselves give an accurate view of their position, this proposal would require multinational companies to publish group accounts relating to all their subsidiaries around the world, in order to make clear the relationships and activities

---

1 OJ L 65, 14.3.1968.
2 OJ L 26, 31.1.1977, pp.1-13
3 OJ L 295, 20.10.1978, pp.36-43.
4 The directive covers mergers both by acquisition of another company and by formation of a new company, and notes that protection of employees' rights in the event of a merger is covered in OJ L 61, 5.3.1977, p.26.
5 OJ L 222, 14.8.1978, pp.11-31.
6 OJ L 100, 17.4.1980, pp.1-26.
7 See OJ C 131, Dec.1972, and Supplement 10/72 of the Bulletin of the European Communities for the proposal.
8 The proposed dual board structure is described on p.75.
9 OJ C 121, 2.6.1976, pp.2-10. Amended proposal: OJ C 14, 17.1.1979, pp.2-23

within the group. While this has also met with some opposition, notably from the multinational companies, the Commission has reported[1] that the positions of Member States seem to be moving somewhat closer on this directive, and that a form of compromise may be possible.

The proposed eighth directive covers the establishment of standard minimum qualifications for auditors of public limited companies.

Proposals for the ninth and tenth directives, concerning the structure of groups of companies and the winding up of solvent companies respectively, had not been published by the end of 1982.

From the point of view of improving company information for shareholders and potential investors, then, the company law directives have been fairly successful. Indeed, it has been claimed[2] that the consequence of the fourth directive is that more than a million companies in the Community will, in future, be presenting comparable annual accounts, which will make co-operation between comapnies in different Member States easier, and should stimulate transnational investment in the Community. However, attempts to harmonise European company law for social ends will, by the experience of the proposed fifth directive, be likely to meet with considerable opposition .

- Harmonisation of Corporate Taxation.

The Commission does not intend tax harmonisation to serve the purpose of instituting a tax policy similar to that applied by the Member States, nor does it see it as an end in itself, but wishes it to be employed as a means to the end of economic integration.

---

1 Bulletin of the European Communities, No. 7/8, 1982, p.17.
2 See D.Evans, p.178

The aim is to use harmonisation of taxes to eliminate distortions in the free movement of capital (such as double taxation). The policy cannot be described as a success so far; of the five proposals presented by the end of 1982, not one has yet been passed.

The reason for this is essentially that no Member State government has so far been willing to surrender sovereignty over taxation rates. This would reduce the variety of fiscal instruments at the government's disposal, and also result in a possible reduction in national tax revenue. Politically, it would be an extremely sensitive issue, since the government would be surrendering the right of the people to 'vote their taxes'.

The proposals put forward so far cover :

1. Harmonisation of corporate taxes and withholding taxes on dividends.[1]
2. The application of the above proposal to dividends received through the intermediary of investment funds or unit trusts.[2]
3. Mergers, divisions and contributions of assets involving companies from different Member States.[3]
4. Taxation of parent companies and subsidiaries in different Member States.[4]
5. The elimination of double taxation in the adjustment of profit earnings between associated undertakings.[5]

Another problem facing the first proposal is that harmonisation of the rates of taxation can be meaningless where the computation of profits for tax purposes varies widely from one country to another. Harmonisation is thus also necessary in definitions of allowable expenses, depreciation, valuation of assets, etc.[6] The Commission does appreciate that

---

1 OJ C 253, 5.11.1975.
2. OJ C 184, August 1978.
3 OJ C 39, 22.3.1969.
4 Ibid.
5 OJ C 301, 21.12.1976, pp.4-7
6 See Easson (1981), p.339 for a fuller discussion on this point.

harmonisation of tax rates and credits must take place alongside the gradual harmonisation of systems of assessing companies' taxable profits,[1] but the European Parliament has delayed discussion on the issue until such time as the Commission can draw up proposals for introducing these changes.

The second proposal is tied to the first.

The purpose of the third proposal would be to defer the taxation which would otherwise arise from a transnational merger or similar operation between Community firms, such as a capital transfer tax or a tax on unrealised capital gains, due to the possibility of assets being transferred abroad, until such time as the assets are realised or the reserves are distributed.[2]

The Commission believes that the effect of this proposal would be to remove some of the tax obstacles to transnational co-operation between enterprises wishing to concentrate or disperse their activities.[3] Serious differences of opinion exist in the Council, however, resulting in deadlock. Problems of differing tax rates feature here, but the principal fear is that the proposal could be used to relocate a company's management outside the Member State in which the head office is situated, and thus avoid worker representation on the company's board.[4]

The fourth proposal has also been held up by the absence of any harmonisation of corporate taxation rates.

Finally, disagreement still exists over the fifth proposal, which aims to eliminate double taxation arising from transfer pricing policies, since the proposal makes no attempt to prevent the actual practice of artificial transfers of intra-group profits across borders through transfer pricing policies.[5]

---

1 See European Parliament Interim Report, 2nd May 1979; Rapporteur: K.Nyborg.
2 See Easson (1980), pp.182-183, for a more detailed analysis of this proposal.
3 Bulletin of the European Communities, No. 4, 1980, point 2.1.32.
4 OJ C 183, 21.7.1980, pp.25-26.
5 OJ C 18, 23.1.1978, pp.27-30.

The European Parliament believes that the only satisfactory solution to the problem of tax distortions will be found in a gradual harmonsation of taxation and, more generally, in the economic and monetary union which is the eventual aim of the Commission.[1]

---

1 See OJ C 163, 11.7.1977, p.25.

CHAPTER THREE

ENTRY STRATEGIES FOR E.C. MARKETS.

Firms may wish to enter EC markets for a variety of reasons, such as market size and growth rate, the need to maintain close contact with customers, or poor prospects in the firm's own market. A firm may expand into a foreign market independently, through an intermediary, through co-operation with another firm, or through acquisition.[1]

The object of this chapter will be to examine the available entry strategies, together with some of the issues involved in planning, setting up and running an operation.

The entry strategies considered here involve:
Agents: Independent individuals or companies who sell goods for a commission, but do not take ownership of the goods;
Distributors: Wholesalers who buy from the manufacturing company and re-sell in the market;
Greenfield ventures/sales subsidiaries: Setting up a new, wholly-owned subsidiary;
Licensing: Selling or leasing production know-how, patents or trademarks for a royalty payment;
Takeovers/mergers: Acquisition of a firm already established in the market in question;
Joint Ventures: Co-operation with another firm in one or more areas of activity.

The main focus of attention will be on joint ventures and takeovers, which form the basis of the survey in this study. In addition to covering the advantages and disadvantages of these strategies, then, this chapter will also consider certain aspects of acquisition and in particular joint venture strategy.

The other issues examined in this chapter will be :
Risk and return: setting financial objectives;
Prior research: deciding whether or not the venture will be viable;

---

1 The alternative of not entering the market will not be examined because the study does not contain a control group.

Structuring the venture: determining ownership and control and setting up the venture;
Problems and conflicts: common reasons for failure.

Agents[1]

The strategy of using an agent is a low-risk one. Investment costs are minimal. The agent's function is to win orders for his principal, who then delivers direct to the customer.

Other advantages for the firm with no experience in the market in question are that it obtains the services of a national with local knowledge of commercial, legal and social affairs and customs, with a ready knowledge of the commercial outlets for the product. It is a means of gaining early market experience for the exporter, and is often used as such. Benefits may be immediate, as there are no setting-up costs involved.

There are,however, disadvantages in using an agent. Unless specifically agreed otherwise, an agent will not normally carry any responsibility for after-sales service or the provision of any technical information or help. All liability is borne by the exporter. Furthermore, success is entirely dependent on the motivation of the agent. If the product is difficult to sell, he is unlikely to spend much time on it at the expense of his more successful products. Similarly, the agent will lose interest if his principal does not provide a full and efficient support service.

In addition, the agent may not possess the resources to fully exploit a market of true potential; and finally, where sales do progress over time, the exporter may find that the agent's commission becomes disproportionately expensive in relation to alternatives such as a wholly-owned sales subsidiary.[2]

---

1 For the application of EC Competition Policy to agents, see pp.54-55.
2 These points are developed by L.S.Walsh, pp.65-66, who also provides an excellent agency selection list and the framework of an agency agreement (pp. 149-55).

Good agents can be difficult to find. Before appointing one, an exporter must be satisfied by the candidate's ability to sell the product successfully, involving the spread of his operations, existing sales outlets and, if necessary, ability to provide a spares/servicing/stockholding facilities.

Arguements against agencies can apply whether the product in question is easy or difficult to sell. In the first case, agents will take a high commission where the exporter could have sold the product himself, since it is easy. In the second case, the agent may have other goods to sell, and will not really try to sell the product. He may then present the excuse that the product is not selling because it does not suit the local market, whereas the real reason may simply be that he is not committed to selling the product. Again, the exporter may do better trying to sell the product himself.

Distributors[1]

A distributor differs from an agent in that by buying from the manufacturer and re-selling in the market he takes ownership of the product. Hence his remuneration is not a commission but the 'turn' - i.e., the difference between his buying and selling prices. The distributor is therefore a wholesaler.

He thus undertakes greater responsibility and commitment than an agent. It is up to him to provide warehouse facilities, maintain inventories - in fact, carry out all the functions normally carried out by a firm selling its own product. Some of these functions may involve some co-operation with the supplier.

The distributor is not restricted to selling the exporter's products, and may have similar arrangements with other suppliers; however, the supplier may be able to prevent the distributor selling competing products, by agreement. In return for this, the distributor

---

1 For the application of EC Competition Policy to distributors, see pp.54-55.

will normally be granted the exclusive sales rights to a given geographic market.

In some respects, however, a distributor presents the same problems as an agent. Again, the key issue can be one of commitment. The distributor will tend to put more emphasis on selling products which are relatively easy to sell and which generate a significant part of his profits than for other products, which thus stand to be neglected. Again, the manufacturer of these latter products may do rather better by trying to sell them himself. It is therefore vital, again, that the exporter should provide the distributor with a full support service, such as technical help.

One question which will be shown in the survey to be important is that of continuity.[1] Either the supplier or the distributor can end a relationship. The willingness of customers to purchase from the distributor often depends on the assured continuing availability of matching equipment and spare parts. In such cases, then, it is vital for the supplier and distributor to be able to display a strong, stable relationship with full support and commitment from both sides.

In practice, a good distributor with adequate sales outlets who does not already have existing and stable commitments may be difficult to find.[2]

---

1 See p.205.

2 R.L.T. Bickers believes that for this reason, for capital equipment and consumer durables, a manufacturer's own operation is the best solution (p.24). The same writer also provides a useful specimen agreement between a principal and a distributor. See also R.E. Ross (pp.83-86) for a list of characteristics and performance functions pertaining to the distributor, together with a list of major factors in determining an exporter's distribution needs.

Greenfield Ventures/Sales Subsidiaries

A greenfield venture involves entering a market by setting up an entirely new manufacturing operation in the country in question. Sales subsidiaries do not require a production base, but only a sales office.

In favour of the greenfield venture is the fact that control is complete - perhaps even more so than in a 100% takeover, since there are no dividend loyalties or wishes to adhere to old values and practices. There may be less time spent in reaching and implementing a decision. In addition, using standardised and known systems and methods throughout the corporate group may result in better internal communication, and speed and efficiency in general. Finally, of course, the profits are not shared with anyone else.

The cheapest form of entry for setting up an overseas sales subsidiary is to form a new company registered in the host country. The firm may thus balance its commitment against its needs in this market. Acquisitions of local marketing organisations are likely to be expensive in terms of goodwill, and the acquiring firm inherits all the other products sold by the previous owners. And the acquired firm still has to be able to adjust to the organisational requirements of the new foreign owner.

A sales subsidiary may be justified where the sales cost per unit is expected to be less than the distributor's margin. Benefits may include : concentration on one product, rather than the wider range carried by a distributor; control over marketing operations; and closer customer contact, including a possibly improved spares and after-sales service.

It has been pointed out,[1] however, that an overseas sales subsidiary is not automatically successful in generating increased sales, and that if the market is limited, uncertain or risky, firms may find agency representation or direct selling more appropriate. But the existence of a proven and growing market may well justify such a commitment.

---

1 Newbould, Buckley & Thurwell, p.198.

An overseas sales subsidiary represents a much smaller commitment than an overseas production subsidiary since the cost of establishment are lower.

Disadvantages of greenfield and overseas sales ventures include:

a) The risk is wholly borne by one party.

b) The firm may suffer from a lack of local knowledge on legal; economic and commercial; social and political affairs and customs.

c) The firm may encounter language difficulties as well as a culture gap.

d) Nationalistic barriers[1] will be more difficult to overcome by entering the market as a foreign firm than would be the case with a domestic partner/intermediary.

A greenfield venture may be forced on the firm because of a lack of suitable takeover victims or joint venture partners, since there may be few available in the product or geographic market within which the firm wishes to operate. In addition, where a takeover is possible the firm may find that to take over a successful company would be expensive, whereas to take over an unsuccessful company, while cheaper, would involve inheriting all the acquired company's faults and problems.[2]

Finally it has been suggested that the new wholly-owned subsidiary would be suitable for firms which have a strong world-wide competitive position based on size, a 'world-beater' product, or any other quasi-monopoly advantage in the form of technology and management, for instance.[3]

---

1 See pp. 202-204.
2 See G.D. Newbould et al., p.75
3 This point is made by S.Gullander (II), p.105.

Licensing[1]

This occurs when a manufacturer sells or leases the use of his patents, production know-how or trademarks to an independent foreign producer in return for royalty payments. Essentially, this means that the manufacturer substitutes an export of technology for the export of his own products.

There are a number of possible benefits to both licensor (the seller of technology) and licensee (the buyer), which are as follows:

Advantages to the licensor :

a) Licensing requires very little investment, and is thus a very inexpensive means of achieving market penetration. There are no labour costs, and licence income is largely pure profit. A minimum royalty income can often be guaranteed.

b) Risk is therefore also very low.

c) Licensing is a relatively easy method of obtaining market exposure abroad. The limited capital requirements involved mean that it is possible, by operating a number of licences, to take advantage of other firms' marketing organisations around the world and thus quickly become international despite having little previous experience abroad.[2]

d) Licensing is a means of circumventing entry barriers such as import restrictions, transport costs, or local preferences to buy from domestic manufacturers.

e) Royalty payments may help to finance the licensor's own expansion programme.

---

1 For the application of EC Competition Policy to licensing, see p.55.

2 See, for example, Jones pp.80-81 and Walsh p.71.

Advantages to the licensee:

a) Expansion of the product range improves its size, risk and profitability. In the case of diversification, the firm can also buy in the licensor's experience of marketing techniques.

b) Savings in research costs and time mean that the licensee can market the product more quickly than if it developed it itself.

c) The licensor does not interfere in the licensee's decision-taking activities, beyond controls determined in the licensing agreement and the power to end the agreement.[1]

d) The licensee can get access to the licensor's continuing development.

e) Payments (royalties) are financed out of cash flow from the new product.

Suitable cases for licensing:

Licensing may be an advantage where :

1. Transport costs are proportionally very high, as in the case of high volume, low value products, so that local manufacture is a distinct advantage.
2. The product demands installation or service support better than an agent can provide, but to which the producer is unwilling to divert resources.
3. Where a product contains high and low value components, the high value units can be exported direct to the licensor, who can add the low value components and assemble the product.

---

1 Dunning suggests (p.404) that from the licensee's viewpoint, this may be the main merit of licensing agreements.

Where a good deal of management involvement is required, however, the licensor may decide that control of the operation can best be achieved by a more direct form of investment.

It is possible that licensing can be used by firms as an important strategy with which to control competition within an industry/market, since licensors can potentially give exclusive rights for particular uses and geographic areas. This control can be entended by the use of cross-licensing agreements. This can bring licensing agreements into the area of antitrust policy.[1]

Disadvantages to the licensor :

a) It is possible that when the licence expires, the licensor may find that it is in competition with the licensee. One of the firms in the present study found that its licensee in West Germany was manufacturing under its own name and competing with the licensor in the USA. The high cost of lengthy legal proceedings deterred the firm from taking legal action. In other instances, however, the firms have become more closely associated and have followed the licence with a joint venture or an acquisition by the licensor.

b) The licensor loses control over production and marketing. He thus has to have confidence in the licensee's ability to fully exploit market opportunities, and to meet his product quality standards.

c) The licensor generally obtains a lower rate of return than would be possible from exporting or equity investment. For licensing to be the preferable route requires the right type of product, such as in an innovative industry in which the licensed right will only be of advantage for a relatively short period of time. For long run manufacturing on any significant scale, it would be more advantageous for the potential licensor to enter the market independently and thus retain all the profits from the venture.[2]

---

1 See Lowe & Crawford, pp.8-9, for a full discussion of the anti-competitive consequences of licensing agreements.

2 See, for example, R.E. Caves pp.272-273, and R.T.Jones p.82.

d) Quality control is difficult. This can cause embarrassment for the licensor, as the product is often sold under his brand name.

e) Disagreements with the licensee. It is important that the two firms share the same objectives. Problems can be minimised by prior negotiation and an extensive licensing agreement.

In certain circumstances, a joint venture may be preferable to a licensing agreement. This will usually occur when the potential licensor wishes to retain a more consultative influence over the way in which his products will be presented to the market. The firm may, for example, wish to ensure high product standards so as to preserve its reputation. In order to gain some management control, then, the firm may ask for equity rather than a royalty fee in exchange for its technology. This may have the additional effect of improving communication links, and hence interaction, between the originating firm and the new venture, and thus aid technology transfer. The awareness that licensing agreements could be improved in these respects has in some cases led to them being replaced by joint ventures.

Takeovers/Mergers[2]

A. Reasons for Acquisitions

1. The purchasing company obtains a ready-made market position. Revenue earning is therefore immediate. The acquisition may comprise production facilities, an established marketing and distribution organisation, market knowledge and contacts, and trained and experienced local staff. The firm may thus quickly achieve

---

1 Checklists for drafting a licensing agreement are provided by Channon & Jalland (pp.199-200), Jones (pp113-115) and Walsh (pp.72-74). Channon & Jalland also provide lists of factors important for success (p.198) and factors leading to failure (p.199) in licensing.

2 For the application of EC Competition Policy to takeovers/mergers, see pp.56-57.

the necessary critical size for it to become an effective competitor. Through acquisition it may broaden its customer base and open new market capabilities. The fact that the acquired company already exists in the market should, in addition, enable the firm using this as an entry strategy to circumvent many cultural, legal, management, and other start-up problems.

Acquisition can, however, result in significant problems. Integration of the acquired firm with the rest of the group may take a long time and produce important human problems.[1] Furthermore, in a comprehensive recent study on mergers and acquisitions, D.C.Mueller et al. concluded that if acquisitions resulted in an increase in market power, they would appear to be offset on average by a decline in efficiency.[2] There is further evidence that motives for acquisitions are predominantly to gain increased control of the market - and hence achieve a reduction in uncertainty - and to defend market and industrial positions.[3]

2. The acquiring firm obtains resources which would otherwise be impossible or costly to gain in any other way - for example, greater product and technical sophistication; management skills; essential marketing skills; research capabilities; improved quality control over a previous licence agreement; improved communication with a previous distributor.

3. Pro-merger theory holds that this strategy results in greater efficiency, and that complementary factors will lead to the earnings of the combined enterprise being greater than those of the separate companies. In

---

1 See pp.116-117, 188-189 and 196.
2 D.C.Mueller (ed.), p.309
3 See the study by G.D.Newbould (1970), p.160

particular, opportunities may be created for excess capacity to be utilised, and economies of scale to be obtained in marketing, production and other areas.[1] This is explained by the notion that the combined production demands, allowing for plant product specialisation, would result in longer production runs and a consequent relative reduction in fixed costs. The end result is held to be greater efficiency, higher levels of economic activity, and a faster rate of growth.[2] This analysis is wholly dismissed by Mueller et al., whose extensive analysis (published in 1981) consistently rejected the economies of scale motive, and further suggested that mergers have not lead to efficiency gains.[3]

4. Acquisition may eliminate a potential competitor.[4]
5. Acquisition may represent a lower risk than a programme on internal development because the acquired firm has already produced known results.[5]

6. The acquiring firm can take advantage of surplus cash of its own, or benefit from a previous tax loss carried forward by the acquired firm, thus reducing future tax liability. Furthermore, the possibility of issuing shares in payment may minimise the actual cash requirement for the purchase.
7. Time can be an important reason for making an acquisition. Through this strategy, a firm can save the development time for a new product made by the acquired firm, as well as the time taken to develop a sales and distribution network and a market share. The firm can also benefit from learning curve effects.[6]

---

1 See pp.169 and 176.
2 See, for example, M.A.Weinberg et al. p.35; T.Fikri pp.291-93; F.R.Root p.41.
3 Mueller pp. 302-308.
4 See p.175.
5 See p.169.
6 The learning, or experience, curve effect is that unit costs decrease as production increases over time, due to improvements in efficiency as the company gains more experience in the manufacturing process. Speed of entry to the market is confirmed by the results of this study as being the most important reason behind the JVs and takeovers in the sample. See pp.173-5.

8. In the case of a vertical relationship, the acquiring firm can ensure raw material supplies or a sales outlet.

9. If there is a falling return on investment in the buyer's own industry then diversification in order to reverse this trend is a possible solution. This strategy will reduce the company's dependence on a limited area of growth and spread its activities to different industries with different business cycles. However, since diversification leads the firm into unfamiliar territory, this may affect not only its original judgement, but also its ability to run the acquired firm afterwards. This may result in an unsuccessful outcome.

10. Financial reasons:

    a) Discounted assets : the firm may be able to acquire the assets or shares of another firm at less than the value which the buying firm places on them.[1]

    b) Discounted earnings: the firm may acquire the right to its "victim's" profits at a lower multiple than the stock market places on the buying firm's own profit. That is, it may acquire a company with a lower share price/earnings per share (P/E) ratio than its own. The effect of this is to increase the purchasing firm's earnings per share (EPS). However, if the rate of growth of the acquired firm's EPS is lower than that of the purchasing firm, this benefit will only accrue over the short run, unless the buyer can, through making more facilities and financial backing available to the new firm, improve the latter's EPS growth rate. Otherwise the effect will be, despite the initial boost, to slow the parent's own EPS growth rate.

A previous study on acquisitions in Europe found that financial reasons were relatively insignificant factors in takeovers.[2] This confirms the view that such operations are undertaken for reasons other than maximising efficiency.

---

1 See p 177.

2 See J.Kitching, pp.188-189

B Disadvantages of Acquisitions

1. 'Good' candidates may not be available. In addition, shortcomings in information may make valuation difficult. Differences in accounting systems, poor company information systems and attempts by the existing management to conceal faults can all contribute to this problem.
2. There is a possibility of over-payment, as it will be in the present owners' interest to overestimate the value of the company and of its assets. The true value really depends on its worth to the acquiring firm. In that the acquisition has yet to be integrated with the rest of the group, this value will be earier to assess after the event, which may be too late.
3. Integrating the acquired company into the firm can be a very difficult process. The two companies may have different methods, philosophies and organisational systems, and attempts at integration can cause resentment and friction. Cultural differences may exacerbate any problems. It is also possible that an emphasis on restructuring of the acquired firm can take precedence over the original intentions of the takeover, and can indeed result in some of the original attractions of the purchased firm being lost.[1]
4. Host government assistance, such as regional grants, which may be readily forthcoming in the case of a greenfield venture are unlikely to apply to takeovers. Indeed, there may well be strong host government opposition to the acquisition,[2] unless the firm can demonstrate that it will not result in a transfer of operations and assets abroad, with a consequent decline in local employment.

---

1 See Hovers p.114, Young pp.42 and 137, Levinson p.66, and Walsmsley p.4 for a more detailed analysis of this problem. Also see the present study, pp.116-117, 188-189 and 196.

2 See, for example, p.215.

C. Who gains ?

Previous research indicates that whereas management may benefit from an acquisition, in general shareholders, employees and the economy do not. Studies by Newbould (1970), Newbould & Luffman (1978) and Mueller et al. (1980 all concluded that mergers do not increase economic efficiency, as evidenced by profit and growth increases. Indeed, Newbould & Luffman went as far as to state that shareholders did progressively worse (in terms of rates of return on their investments and capital losses on their shares) the more heavily their companies pursued a policy of acquisition, and best with companies that relied entirely on internal growth.[1]

These results conflict with neoclassical theory of merger outcomes, and indeed with the traditional perception of management's role in profit maximisation. Acquisition strategy appears instead to be based on management motives. These may stem from feeling of achievement, status and prestige that controlling a larger company may bring. It may be that management remuneration increases with firm size, in line with responsibilities; increasing the size of the firm may make it less susceptible to being taken over itself; or, alternatively, acquisitions may simply be made as being the most convenient way of entering a market.[2]

D. Acquisition Strategy

The best means of formulating an acquisition strategy is this:
Having decided on the market to be entered, the firm should first conduct an extensive self-examination, in order to find out to what extent it could enter the market on its own. If it is decided that this would raise some difficulties, the firm should then identify its specific shortcomings, which may be the lack of an established distribution system, people with a detailed knowledge of the market in question, time or finance. It can then decide if it can overcome these problems

1 See Newbould & Luffman, p.55
2 See p.178.

by, say, employing suitably qualified local nationals.

This self analysis means that when the firm eventually gets round to looking at local firms for acquisition/ co-operation, it can identify the most suitable ones by the specific characteristics of which it is short. Only then should it decide on the most appropriate stategy. The most suitable firm may, for example, not be available for take-over, but may be willing to enter a co-operation agreement. It may well be better to have a part share of a successful operation than 100% of a less successful one.[1] The strategy of acquisition should thus be considered along with other strategies, with the most appropriate one chosen to fit the circumstances.

A previous study of transnational acquisitions in Europe has concluded that the chance of success mounts in direct relation with the share of the market purchased, and with the profitability of the target company. Kitching's analysis found that European acquisitions are characterised by a high failure rate, with 21.6% of cross-border acquisitions involving only European firms being classified by the companies concerned as 'failures', and with a further 27.4% being 'not worth repeating'. That is, the success rate in his sample was only 51%. The study concluded that the key factor in developing an acquisition strategy is to do everything possible to ensure increased market share, earnings per share growth, and sales growth.[2] The fact that so many firms in Kitching's study did not pay sufficient attention to these factors implies that where firms have failed, it is generally due to inadequate planning. The present study will develop this theme further.

---

1 See p. 197.

2 See Kitching, pp. 193-204, and also the present study, p.179, for comparative results.

Joint Ventures

A Advantages of JVs

Joint ventures (Jvs) are another means of penetrating a new geographic or product market. In many ways, the reasons for using this strategy are essentially the same as those for takeovers, in that they entail an implicit recognition of the fact that the firm is unable to achieve its aim with its own resources alone, and that some form of collaboration would offer a better solution. The main difference between the two stragies is that a joint venture involves giving up a share of the profits, in return for a reduction in the risk. Another important difference is that a JV involves co-operation rather than the control and subjection of one management to another which occurs in a takeover. The JV possesses an inherent flexibility in that it can be designed to suit the individual requirements of the companies in question.[1]

Some of the potential benefits may be :

1. Access to technological information or local cost benefits.
2. Local management skills, including knowledge of legal, economic, social and political affairs and customs. This may be particularly useful in a first incursion into the market in question.
3. The addition of another marketing force means that the firms can take advantage of production economies of scale which would otherwise have resulted in difficult marketing problems.[2]
4. By pooling its resources with another company and sharing project and capital costs, a firm may be able to undertake a joint project with would be beyond its own financial resources.[3]

---

1 See Walmsley, pp.3-5, on this point.
2 See pp.169 and 176.
3 See pp.18 and 66.

5. Spreading the risk of loss of capital.[1]
6. Strengthening a vertical relationship through, for example, assuring a source of supply. A JV can also be profitably used where, for example, the firm sees a distributor with a good marketing network and after-sales service in trouble because it is under-capitalised or because the quality of its present products is inadequate.[2]
7. Speed of entry into the market through acquiring immediate marketing expertise or a distribution network.[3] In addition, a JV partner may be more committed to the success of a project than may an agent or distributor with a variety of conflicting interests.
8. The firm can expand its product line or by diversifying avoid cyclical/seasonal instability.
9. In some overseas markets, joint ventures are forced upon a firm by government legislation. Although this is not the case in the EEC, in sectors in which the government or a state industry is a major customer, pressures on a foreign firm may be severe unless there is some form of local involvement. Other customers may also have nationalist preferences which the JV may help to assuage.
10. JVs are useful where the firm wishes to invest in a number of countries at the same time and hence needs to limit the capital investment in each.

In a study by Stopford & Wells, 99 U.S. multinational corporations placed the importance of the JV partners' contributions in the following order :[4]

1. General knowledge of local economy, politics, customs.
2. Speed of entry.
3. General managers.
4. Access to market for local goods.

---

1 See pp.169 and 176.
2 For an extension of this point see Bickers, p.28.
3 See p. 174.
4 J.M.Stopford & L.T.Wells , p.103

5. Marketing personnel.
6. Capital.
7. Access to local raw materials.
8. Production, personnel, R & D skills.
9. Access to market for foreign goods.

It should be noted that these firms were large multi-nationals involved in JVs all over the world, and as such were often involved with non-technical local partners. This may account for the relatively low importance given to the partners' technical abilities. In the EEC, it is likely that both partners may contribute technology, and the importance attached to the technical ability of the partner is consequently expected to feature much more strongly in reasons for collaboration.

Finally - and this is what most concerns the European Commission - it is possible that firms may enter JVs in order to eliminate competitive uncertainties; that is, to substitute a 'negotiated' business environment and degree of competition for a more free market structure. Smaller firms may opt for such agreements in order to protect themselves from severe competitive pressure from large oligopolistic companies, by whom their existence may be threatened.[1]

8 Disadvantages of JVs

By entering a JV, a firm gives up a share of the profits of a venture, although it is possible that this part share could still be more than the full share of a wholly-owned route, depending on how successful the different strategies would be.

Another problem is the loss or dilution of management control. This can be crucial issue where one or both partners wants the JV to behave in line with group policies, instead of as an independent entity. This will create clashes between the partners if one firm attempts to maximise its own profits from the venture at the expense of the JV itself - for example, by manipulating transfer prices or attempting to prevent the JV from competing with another subsidiary in export markets. A difference in

---

1 See p.199.

attitudes to risk and short term cash flow can also cause disagreements where, for example, one partner is willing to sacrifice short term profits in return for an increase in market share.[1]

A further drawback is that in entering a JV, a firm may be helping its partner to become a stronger competitor in the future, especially where a transfer of technology is involved with a partner who possesses the capital resources to exploit it.

Other difficulties for a tansnational JV may arise from differences in legal, fiscal and accounting systems; differences in business practices; communication problems arising from language and cultural differences; and EEC antitrust legislation which requires JVs between firms above a certain size to be notified to the European Commission.[2]

C Joint Venture Strategy

Joint venture strategy should be formulated in essentially the same way as acquisition stragegy, with an analysis of the firm's aims and requirements being followed by an examination of the market and of the available entry strategies. The JV path should then be followed where in the circumstances it is deemed to be the most attractive means of market entry.

In addition to the JV aimed at market entry or at achieving economies of scale, this strategy may also be used where firms wish to become more closely integrated through a merger, but wish to eliminate some of the uncertainties about whether or not their organisations are compatible. This can permit a period of adjustment and working together without making an irreversible commitment. The JV may, of course, itself be a form of further integration, possibly resulting from an earlier distribution or licensing agreement between the firms concerned.[3]

---

1 See Channon & Jalland, p.202 for a further development of this issue.

2 See Appendix 2 on 'block exemptions'.

3 See Gullander (I) pp. 106-109 for suggestions of three different types of JV strategy: a networked system of JVs; the standard short term JV; and the successive integration strategy.

This chapter will now examine characteristics of JVs and of the potential parents themselves which may influence their decision whether or not to use this strategy :

a) Firms attracted to JVs

- technological firms: Such firms may be attracted to JVs if the technical sophistication of their products is such that a single national market would be inadequate to exploit it, and they do not have the financial capacity or international structure to do so. This can also be done through a licensing agreement; but many firms prefer an equity stake to a straight royalty payment.[1]

- diversified firms: The firm with highly diversified products may be short of an organisational back-up structure for some of those products. It may therefore need help on marketing and distribution in the foreign market, together with local management knowledge. A JV with a local company providing such facilities would thus help the firm enter the market much more quickly than it could do otherwise. Speed of entry is thus expected to be an important reason for collaboration.

Kitching has found that diversification into new products via a transnational takeover in Europe is negatively correl ated with success.[2] Introducing a new product abroad through a JV, however, reduces the risk and also the firm's exposure to many of the possible organisational problems.[3]

- small single-product firms : Such firms may not have the financial strength for either an independent expansion or a

---

1 Killing (I) pp. 43-46 gives further details of the JV requirements of high-technology firms.

2 See Kitching, pp. 61-72.

3 See Brooke & van Beusekom p.119; Gullander (II) pp.106-7; Franko pp.5 and 72; and Stopford & Wells p.68, for a discussion on the suitability of JVs for the diversified firm.

takeover, and may thus see JVs as a means of achieving the size advantages of economies of scale or critical mass (necessary minimum input level) required for a project. The same situation may apply to divisions or subsidiaries of large diversified firms who may have management autonomy.[1]

b) Firms against JVs

- large single-product firms: These firms do have the financial strength for an independent expansion. Their size and specialisation is such that they are unlikely to require technical help and should be fully conversant with the requirements of their customer group. A study by Franko has found, in fact, that such firms find sooner or later that they cannot live with JV partners.[2]

- marketing-oriented firms: Firms which specialise in marketing techniques are unlikely to take kindly to interference by a JV partner with its own marketing skills, and clashes over policy would be likely in the case of a JV. Moreover, such a firm is likely to be confident about exposure to the market and would not be expected to require the assistance of a local firm. It may, however, be willing to consider a JV which involves marketing another firm's products.

- production rationalisation firms:[3] Such a firm will wish to make a JV conform to group policies rather than to behave as an independent entity. The firm will allocate production among its subsidiaries and co-ordinate their marketing operations so as to maximise the profits for the group as a whole. This approach will make severe conflicts with a JV partner inevitable. The partner - who may also wish to use the JV for his own ends - will at least want to maximise JV profits. This means that he will strongly oppose any attempt-

1 This point is extended by Gullander (II), p.107.
2 See Franko, p.5
3 See also p.187.

by the firm to re-allocate production to another part of the group, or any attempts to constrain the JV's export potential where it might compete with one of the firm's other subsidiaries. The policy objectives would thus be incompatible, and such firms therefore tend to avoid joint ventures.

c) Firm size differences

Where significant differences exist between the sizes of the partners, this may result in the JV being much more important to the smaller firm than to the larger one. The small firm may thus wish to give far more time and attention to the needs of the JV than the large company. Where additional resources are called for, however, the smaller firm may be less able to afford an increased contribution. This may put pressure on the larger firm to buy out the operation, or at least to take an increased share.[1]

d) Shared or dominant management ?

For a dominant partner, this may be more likely to result in consistency of policy, and hence less uncertainty about the JV. Of course, the reverse may apply for the minority partner. From the point of view of the firm entering a foreign market, a majority (large enough to determine policy) JV gives it the advantages of control together with the benefits of local participation.[2] A problem for the minority partner, however, is sustaining the motivation to work in the JV, particularly if it is unable to have an influence on policy.

---

1 See p. 205.

2 Newbould, Buckley & Thurwell found (p.74) that for these reasons firms are likely to find ownership of between 75% and 99% of an overseas subsidiary the most successful structure. Killing recommends (II, pp.121-7) that shared management should only occur where the continued operational involvement of both firms, as opposed to a one-off transfer by one firm, is necessary.

e) Risk

Levels of risk may vary between the partners. For example, a firm contributing technology may place the same value on its input as a partner contributing cash. However, the firm putting up the finance is the one which is taking the greater financial risk, and its attitude is bound to differ.[1]

f) Planning[2]

There is no substitute for extensive planning for a JV, or indeed any other venture. The firm should ensure that all potential problems are ironed out before the venture starts. It is far better for a JV to fail in the planning stages than after it has started, and resources have been committed. While flexibility is necessary, a JV cannot work where the true objectives of the partners are incompatible. It is essential that both firms should be prepared to enter frank discussions about their aim, so as to agree on objectives, which should be included in the written JV agreement.

Risk and Return

Risk is defined as 'a condition under which either the occurrence or the outcome of alternatives is not certain but is assigned probabilities'.[3] The difference between risk and uncertainty is that the latter is unmeasurable.

---

1 See p. 188.
2 See pp 108-111 and 193-194.
3 The definition is that used by Ansoff, p.155n.

If a firm is to invest in an alien environment involving greater uncertainty, and therefore risk, than it faces in its present markets, it should demand a higher return from its investment than it could obtain by expanding its present operations, to compensate for this. Otherwise it would be better off investing in its current markets, where it has a detailed knowledge of the business environment.

Rates of return on overseas investment should, however, be compared with marginal returns on domestic investment, rather than with existing average returns. Where the home market is saturated, for instance, marginal returns will approach zero, and the only possible room for expansion (in the same product market) will be overseas.

A previous study of overseas production investments found,[1] however, that over half the firms in the survey had invested abroad without setting any financial objectives for the investment. It concluded that the firms which did set financial objectives were on the whole more successful than those which did not.[2] This is only to be expected, since not all the proposals subjected to risk analysis would have been accepted as being viable or worthwhile propositions, and some would consequently have been dropped.

Essentially, risk analysis depends on the original background research.[3] The more research is done, the more will be known about local economic, industry and business factors and their effects on the variability of cash flow and return on investment. The firm can thus make more effective estimates of market share and growth performance. Other factors must also be borne in mind - for example, a change in exchange rates can put great pressure on a foreign investor and place an entire venture in jeopardy.

---

1 Newbould, Buckley & Thurwell, p.111. 40% of the participants in the present study also carried out no financial planning for their ventures (see pp. 206-207).
2 Similar results were obtained in the present study (see pp. 206-207).
3 See, for example, pp. 207-208 of the present study.

The exchange between prospective gain (return on investment) and risk is a subjective matter and can only be left to the individual decision-maker to judge.

Prior Research

The purpose of prior research is to increase market knowledge, thereby reducing uncertainty and hence risk.[1] The firm which is not concerned with undertaking prior research is not interested in reducing its risk. It is difficult to see how this can result in anything but harm to the firm in the long run.

If a proposed venture is going to be successful, it is possible that the non-researching firm will make a slightly greater profit than the researching firm because of the latter's additional research expenses; although it is possible that this research will have led to strategic modifications resulting in a larger profit overall. But in the case of a proposed venture which (although not known at the time) is going to be a failure, the non-researching firm stands to lose its entire investment. The researching firm, on the other hand, has a good chance of identifying the weaknesses of the project during the research stage, in which case it would lose only its research expenses - very minor in comparison with the non-researching firm.

The cost of the research is a few weeks' work and a comparatively small amount of money. The potential savings must heavily justify the expense.

Despite this, the study by Newbould et al. found that 60% of the firms covered sought no market information other than what they already knew from exporting to the market in question or having an agency or sales subsidiary there.[2]

---

1 See pp.207-208.

2 See Newbould, Buckley & Thurwell, p.88, and also the present study pp. 106 and 179-81. The need to do sufficient background research was the main lesson learned by the participants of the present study (see pp.193-194).

The prospects for success in a JV can be helped by the sharing of research by the prospective partners. This joint operation will help to identify any problems both in the product/industry and in any working relationships between the two firms. It will help to develop common targets and enable both companies to demonstrate their commitment to the project before finally committing their resources.[1]

This research will be considered under the headings of : (i) the country; (ii) the prospective partner/victim; (iii) the industry; and (iv) the product.

(i) The Country: Examples of issues to be examined here are :

- Taxation;
- Size of GNP and growth rate - in a country with a healthy economy and fast GNP growth rate, the chances are that the venture will also do well;
- Inflation rate;
- Local sources of finance;
- Control rights conferred by certain percentage shareholdings;
- Labour laws;
- Regional investment policies.

Where government inducements are offered, it should be remembered that this is usually for a good reason: there may not be an adequate transport network; the region may not be economically developed; there may not be a suitably trained local labour force. Any such investment decision should therefore be able to stand on its own merits, since the firm has to ensure that it can still run the venture as a profitable concern after the government incentives have weakened.[2]

---

1 See Hlavacek & Thompson p.39 and Walmsley p.69 on the virtues of undertaking joint research.

2 These views are confirmed by the results of the Newbould, Buckley & Thurwell study. pp.118-19, and by Walmsley, pp. 63-64. Comments on this point in the present study may be found on p.213.

(ii) The Prospective Partner/Victim: An initial self-analysis means that the firm can identify potential partners/victims by the specific characteristics which it requires. A number of questions still need to be asked, however. The firm needs to know whether or not the partner can pull his own weight, and whether or not the two organisations will be compatible. Examples of topics which might be investigated are :

- The potential victim/partner's financial performance and current position - profitability, capitalisation, etc.
- Structure of the organisation, information and accounting procedures; is the firm run by an owner-manager ?[1]
- Market position : level of, and changes in, market share; reputation; market practices; vertical relationships - e.g., dependence on one customer or supplier.
- Quality and efficiency of production; investment and innovation; capacity utilisation.
- Possibility of language problems.

In order to gain a clear understanding of the firm's market position and commercial relations, it may be necessary to conduct interviews also with suppliers and customers, who may have criticisms of the potential partner's organisation or products which the partner itself may not mention. The purpose must be to leave as little as possible to chance.

Previous research has indicated that larger companies spend more time on prior research than smaller firms because their size enables them to carry out a more rationalised approach and search procedure.[2] This is only to be expected, since smaller firms are unlikely to be able to afford the same commitment of financial resource or management time to such research.

---

1 See pp 189-192.

2 See Hlavacek & Thompson, pp. 39-40, and Newbould et al., pp.60-61; also the present study, pp.38 and 194.

(iii) The Industry : The firm needs information on such issues as :

which are the leading products and why;

levels and trends in profit margins;

strength of competition and market shares;

number and strength of customers;

the importance to customers of : price; delivery; reliability; quality; after-sales service;

customer attitudes to foreign companies;

growth rate;

technology and trends;

investment;

marketing techniques and organisation.[1]

(iv) The Product : Finally, an analysis of the product concerned should cover such points as :

the purpose of the product;

advantages/disadvantages compared with competing products;

the level and price elasticity of demand for the product;

substitutability of other products;

the level of servicing required.[2]

---

1 A more extensive outline for industry analysis is provided by Ansoff, p.126.

2 More detailed checklists covering all these subject headings are provided by: B.I.M.; Bean, pp.150-153; Hovers, pp.133-55; Walmsley, p.68; Williams, pp.34-38; Young, pp.173-77. Walmsley also recommends that the research should include a detailed feasibility study to assess the viability of the venture.

Structuring the Venture

a) Determining percentage shares

1. Outright control may be achieved with ownership of over 67% in France, and over 75% in West Germany. In France, however, one should not initially acquire more than 80% of a local company, transferring the remainder after the fifth anniversary of the original purchase. The purchasing company is otherwise liable to pay a registration tax of 16.6% of the 'goodwill' value involved in the transaction, or 17.6% TVA (VAT) on the level of stocks held by the acquired company. This liability is at the discretion of the French tax authorities.[1]

   Newbould, Buckley & Thurwell's study of first overseas production subsidiaries found that 75% - 99% ownership was the most successful, since it combines outright control with the benefit of local participation and knowledge.[2] The problem with this approach is that a strong partner may not agree to such a structure, whereas a firm which will agree to it may not be in a strong position. Moreover, outright control can lead to decisions being imposed rather than agreed, which can seriously affect relationships between the firms concerned.

2. Management control, giving the right to nominate management and control the day-to-day activities of the company, is typically achieved with 51% of equity.

3. 50/50 JVs[3]: This structure can be both an advantage and a disadvantage. In favour of the 50:50 JV is that it can create a spirit of true co-operation and equality, whatever the respective sizes of the parents. It also means that decisions must be taken by mutual agreement. Both partners are protected in this respect. However, this also means that in a deadlock situation no decision can be taken. The EC Commission fears, in fact, that this power of veto

---

1 See p.214.
2 See Newbould, Buckley & Thurwell, p.74.
3 See also pp 61 and 217-218.

may restrict the partners' ability to act independently on any matter of importance relating to the JV.

A 50:50 equity split does not necessarily represent the proportions of monetary or physical assets contributed by each parent. This depends on how the different inputs are valued. A firm supplying technology, for example, may be in a strong bargaining position for equity, even though the partner supplying finance may be taking the greater risk.

4. Minority rights, or 'minorité de blocage', apply with ownership of at least 25% of the equity in West Germany, and 33% in France. Shareholdings of this order give the right to prevent changes in fundamental aspects of the business, such as the articles of association, the nature of the business, divided policies, asset liquidations, etc.

b) Ownership and control[1]

The key reason for wanting management control is to be able to influence JV decisions in all aspects of strategy, so that it can fit into a general corporate plan. Thus issues such as transfer pricing policies and competition with other parts of the corporate group can be designed to suit the parent company rather than the JV directly. It has been suggested that for a corporate group united by centralised policies in production and marketing, such control over the JV may determine whether it can be integrated at all in the group.

There are different means of retaining management control. The firm may have the right to appoint directors and managers of the JV; it may issue two types of share - voting and non-voting - and retain a majority of the voting shares. It may hold options to increase its equity stake; and so on.

---

1 See pp. 217-220.
2 See Gullander (I), p.110.

In the case of an acquisition, the acquiring firm has to decide whether or not to retain the former owners/managers. It is true that they will know the acquired firm better than anyone else; however, they may also prefer to continue running the firm on their own. This may be reflected in an unwillingness to conform to group headquarters. Former owner-managers may have vested interest in company policies and may thus be unlikely to respond kindly to parent company interference. In order to ensure an accurate flow of information, the parent may decide to put one of its own accountants into its new subsidiary.

In doing this, however, there is a danger that the new parent might alienate the management of the acquired firm by denying them the autonomy to which they have been accustomed. The effect of imposing control sytems might thus be to stifle the very quality which the acquiring firm had sought to obtain.

The integration of subsidiary staff into the parent company can be a difficult process which may leave much room for misunderstanding. Effective integration requires a common understanding of the strategies, targets and systems of the corporate group. The new parent must consequently be prepared to help the staff of the acquired firm to understand their role and invite them to make a positive contribution.

c) Nationality of the chief executive

The choice here is usually between a national of the parent's country (i.e., the UK in this study) and a local national.

The advantage to a UK firm of using one of its British employees abroad is that communications can be greatly improved, and the chief executive will willingly institute a full reporting system, providing the parent with greater information. He will know how the parent operates and is far less likely to oppose group strategy which will reduce the profitability of the venture in favour of the group as a whole - for example

on transfer prices, rationalisation, or competition with other members of the group.

In favour of the local man will be his understanding of the local market and of local commercial, economic, legal and social factors, together with his language ability. In the acquired firm he may be a former manager, and will be well acquainted with the firm and its products and procedures.

Whoever the parent company decides on, language must be a vital factor. The chief executive must be able to grasp for himself what is happening in the market, and it would be unreasonable and indeed impolite to expect customers and suppliers to deal with the firm in a language other than their own. In addition, however, he must be able to communicate clearly and effectively with the parent company. He therefore needs to speak both languages.

d) The JV agreement.

A well constructed agreement may save enormous subsequent problems.[1] Although flexibility is certainly necessary in a JV, the initial spirit of co-operation is not itself sufficient. This concord may last only until the first clash of interests arises, and then wither away. Once an agreement is signed, both partners can, if they agree, choose to ignore it entirely; but when a potential argument developes, it provides something valuable to fall back on.

As far as is practical, the agreement should cover all possible future disagreements. It requires a clear statement of the objectives of the venture, and agreements on : future growth and profit objectives; duties and obligations; dividends; pricing policies; transfer pricing; competition between the JV and the parents in export markets; product quality; accounting practices; and so on. Discussions should be quite frank. There is no

---

1 See also pp. 38, 46, 194 and 218-219.

reason to conceal true intentions, since this can only lead to future disagrements. If the partners cannot agree on an issue before they are financially committed, the chances of their doing so gracefully afterwards must indeed be slim.

The agreement by itself is not enough, of course. The success of a venture depends on the motivation of the people involved, and personalities can count for far more than paper.

Problems and Conflicts[1]

These can arise from any issues not adequately covered by the written agreement, and are usually the consequence of inadequate planning of the venture. They therefore serve to stress how vital it is for firms to be quite clear about the objectives of the venture and to commit themselves to a written agreement rather than to rely on flexibility and co-operation to solve problems as they arise; they may well find that they are less flexible than they originally supposed.

Inadequate pre-planning may be reflected in: insufficient market/product/country/partner analysis; higher costs than anticipated; poor timing; insufficient investment; stronger competition than expected; unexpected weaknesses in the partner/victim; lack of preparation for integration with a new subsidiary, and so on. In short, it adds to the risk.

A lack of flexibility may result in: difficulties between two incompatible management systems; inadequate support for the venture; insufficient time given to the venture.

Finally, there is the potential problem of 'identity' for an

---

1 See pp. 181-192.

acquired company. This arises where, following a takeover, the new parent imposes its business systems and substantial reporting requirements on the subsidiary, removes its policy autonomy and requires it to perform for the benefit of the group as a whole rather than as an independent entity. This is likely to alienate the subsidiary employees and may well result in many of the original attractions of the takeover being lost. Motivation of the subsidiary managers is likely to be seriously affected, since they will have lost control over their own destiny. They may question their own value in an organisation which is now effectively managed by someone else, and may be unwilling to carry out dictated policies.[1]

These problems can be avoided by helping the subsidiary employees to feel that they are part of the larger group, and inviting them to make a contribution. This means showing these managers that the parent can provide more support and financial backing than was previously available. A group consciousness cannot be imposed, but in a well planned and sympathetic integration subsidiary employees will develop this themselves.

---

1 See pp. 96, 188-89 and 196.

CHAPTER FOUR

THE MECHANICAL ENGINEERING INDUSTRY

This chapter does not seek to provide a complete review ot the mechanical engineering sector. Its purpose is merely to pick out certain features of the industry which may be expected (from the literature) to have a bearing on transnational business co-operation and which will later be developed in the questionnaire.

Although some comparison is made with the UK's principal competitors in this product area, the general approach will be restricted to the UK.

Topics to be covered in this chapter will be :

1. The UK's performance in trade
   - Imports and exports;
   - Price performance;
   - Market shares;
   - Unit values.
2. Investment abroad;
3. Concentration;
4. Profitability;
5. Non-price factors in export competitiveness.

Much of the chapter is concerned with the first section, which through examining the importance of trade in this sector together with the UK's international performance shows the necessity for British engineering firms to be able to perform well abroad, and the difficulties with which they have been presented in international competition. The effects on market performance of exchange rate fluctuations and relative unit labour costs are described.

The second section briefly analyses direct investment flows between the UK and the EEC, while the third and fourth sections examine the structure of the industry and competitive pressures within it, which could lead to firms investing in other markets. The final section is concerned with non-price demand factors which can explain price differentials.

1. The UK's performance in trade

- Imports and exports

Engineering features very strongly in UK trade. Table 14 shows that in 1980,[1] machinery and transport equipment[2] accounted for 25% of UK total imports and 35% of exports. West Germany's strength in engineering is demonstrated by the fact that this sector accounted for 44% of her exports, but only 19% of her imports.

It is interesting to note from Table 15 that while West Germany's imports of machinery and transport equipment in 1980 were, at 25.2 billion ECUs (22% of the EEC total), only 16% higher than those of the UK (19% of the EEC total), her exports were vastly (117%) greater at 61.5 billion ECUs (39% of the EEC total) compared with 28.4 billion ECUs (18% of the EEC total) for the UK.

72% of the EEC's imports in this product sector and 86% of exports were accounted for by W.Germany, the UK, France and Italy.

TABLE 14 Trade in Machinery and Transport Equipment, 1980.

	% of EEC M&T imports	% of M&T exports	M&T as % of total imports	M&T as % of total exports
Belgium/ Luxembourg	10	6	22	22
Denmark	3	2	21	24
France	18	17	21	33
W.Germany	22	39	19	44
Greece	2	0	36	3
Ireland	2	1	27	18
Italy	13	12	20	33
Netherlands	10	6	20	17
UK	19	18	25	35
EEC	100	100	21	33

Source: figures derived from 'Eurostat Review 1971-80', EEC Statistical Office, Brussels/Luxembourg, Nov. 1981.

---

1 Most recent available EEC statistics.
2 SITC Order 7, which includes electrical and instrument engineering and transport equipment besides mechanical engineering.

Table 15 EEC Trade Data

(Mio ECU)

	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1980/1979	1980/1971
6.1.1. Total imports — Importations totales — Invoer totaal											1979 = 100	AM
Belg./Lux	12 357	13 812	17 910	25 015	24 819	31 715	35 418	38 095	44 053	51 632	117	17,2
Danmark	4 343	4 513	6 334	8 331	8 383	11 093	11 616	11 422	13 670	14 106	103	14,0
BR Deutschland	34 431	35 827	44 106	58 046	60 442	78 912	88 803	95 405	116 310	135 243	116	16,4
Ἑλλάδα	2 002	2 091	2 787	3 694	4 301	5 426	5 999	6 150	7 028	7 634	109	16,0
France	20 262	23 818	30 042	44 293	43 682	57 647	61 785	64 215	77 705	97 102	125	19,0
Ireland	1 761	1 877	2 263	3 193	3 046	3 764	4 728	5 591	7 175	7 999	111	18,3
Italia	15 298	17 218	22 649	34 438	31 122	39 485	42 132	44 278	56 716	71 813	127	18,8
Nederland	14 624	15 466	19 799	27 847	28 389	35 832	39 970	41 532	49 053	55 369	113	15,9
United Kingdom	22 915	24 848	31 562	45 347	42 905	50 122	55 522	61 638	74 746	85 853	115	15,8
EUR 10	127 994	139 470	177 452	250 294	247 089	313 996	345 973	368 326	446 486	526 551	118	17,0
España	4 739	6 058	7 786	12 942	13 106	15 618	15 578	14 648	18 521	24 645	133	20,0
Portugal	1 698	1 949	2 451	3 726	3 078	3 782	4 341	4 076	4 774	6 683	140	16,4
Sverige	6 751	7 229	8 830	13 947	14 080	17 528	17 624	16 132	20 941	24 067	115	15,2
USA	43 487	49 549	56 405	84 679	78 098	108 933	129 564	135 985	151 119	173 231	115	16,6
Nippon (Japan)	18 807	20 933	31 021	52 075	46 635	57 995	62 570	62 254	80 708	101 346	126	21,0

6.1.2. Total exports — Exportations totales — Uitvoer totaal												
Belg./Lux.	12 184	14 404	18 203	23 704	23 193	29 340	32 891	35 204	41 033	46 459	113	16,0
Danmark	3 412	3 869	5 083	6 464	7 024	8 139	8 816	9 224	10 786	12 195	113	15,2
BR Deutschland	39 141	41 634	54 397	74 753	72 666	91 155	103 316	111 340	125 243	138 787	111	15,1
Ἑλλάδα	632	776	1 159	1 702	1 855	2 295	2 411	2 645	2 841	3 728	131	22,0
France	19 576	23 042	28 902	38 469	41 981	49 915	55 667	60 116	71 510	80 150	112	17,0
Ireland	1 257	1 441	1 727	2 226	2 585	2 992	3 852	4 459	5 220	6 101	117	19,2
Italia	14 465	16 583	18 105	25 557	28 240	33 504	39 688	43 942	52 615	56 115	107	16,3
Nederland	13 468	15 045	19 511	27 745	28 593	36 149	38 283	39 292	46 434	53 184	115	16,5
United Kingdom	21 423	21 708	24 795	32 373	35 288	41 458	50 276	56 090	66 042	82 063	124	16,1
EUR 10	125 557	138 502	171 862	232 993	241 425	284 947	335 200	362 314	421 704	478 783	114	16,0
España	2 805	3 390	4 188	5 942	6 192	7 806	8 942	10 250	13 276	14 956	113	20,0
Portugal	988	1 148	1 491	1 890	1 556	1 618	1 772	1 905	2 543	3 331	131	14,5
Sverige	7 130	7 815	9 881	13 317	14 007	16 479	16 736	17 081	20 132	22 249	111	13,5
USA	42 119	44 374	57 918	82 592	86 714	102 855	105 303	112 736	132 639	158 514	120	15,9
Nippon (Japan)	22 982	25 546	29 937	46 563	44 934	60 123	70 800	76 593	75 003	93 069	124	16,8

6.4.8. Machinery and transport equipment : imports — Machines et matériel de transport importations — Machines en transportmiddelen invoer												
Belg./Lux.	3 275	3 887	4 841	6 597	6 324	7 996	8 940	9 850	10 749	11 554	107	15,0
Danmark	1 280	1 295	1 826	1 993	2 295	3 139	3 105	3 301	3 336	3 022	91	10,0
BR Deutschland	6 393	6 895	7 880	8 633	10 533	14 128	16 993	19 649	22 455	25 242	112	16,5
Ἑλλάδα	907	857	1 063	1 035	1 531	2 223	2 740	2 526	2 691	2 745	102	13,1
France	5 210	6 257	7 772	9 335	9 613	13 383	13 943	14 911	17 504	20 738	118	16,6
Ireland	472	506	611	700	748	956	1 266	1 670	2 069	2 180	105	16,5
Italia	3 134	3 575	4 485	5 335	5 649	6 955	7 618	8 539	10 349	14 467	140	18,5
Nederland	3 555	3 692	4 610	5 709	6 483	7 603	9 189	9 932	10 993	10 951	100	13,3
United Kingdom	4 023	5 225	6 556	7 655	8 075	10 279	12 588	16 019	19 678	21 729	110	21,0
EUR 10	28 249	32 191	39 644	45 992	51 249	66 663	76 482	86 397	99 824	112 628	113	16,8
España	1 146	1 603	2 193	2 690	2 872	3 582	3 080	2 845	3 505	4 352	124	16,0
Portugal	554	677	823	1 001	779	953	1 140	1 131	1 192	1 656	139	12,9
Sverige	2 077	2 328	2 754	4 011	4 568	5 318	5 505	4 839	5 798	6 441	111	13,4
USA	13 270	15 512	17 671	20 710	19 540	29 824	31 797	37 373	39 162	45 849	117	14,8
Nippon (Japan)	2 140	2 118	2 140	3 599	3 083	4 086	3 730	4 485	5 330	6 026	113	12,2

6.4.11. Machinery and transport equipment : exports — Machines et matériel de transport exportations — Machines en transportmiddelen uitvoer												
Belg./Lux.	2 556	3 306	3 896	4 442	5 405	7 210	7 963	8 534	9 430	10 026	106	16,4
Danmark	907	1 069	1 359	1 774	2 040	2 227	2 330	2 316	2 604	2 951	113	14,0
BR Deutschland	17 655	20 101	25 439	31 766	33 767	43 275	49 422	52 051	56 139	61 506	110	14,9
Ἑλλάδα	11	18	26	45	72	112	127	81	97	114	118	26,0
France	6 586	7 719	9 341	11 403	15 197	18 713	20 769	21 543	25 572	26 534	104	16,7
Ireland	75	119	171	224	288	408	568	618	838	1 128	135	35,0
Italia	5 082	5 856	6 275	8 122	9 842	11 440	13 355	14 364	16 219	18 348	113	15,3
Nederland	2 534	2 968	3 676	4 609	5 397	8 892	7 161	7 351	8 114	9 053	112	15,2
United Kingdom	8 987	9 378	9 506	11 887	14 706	16 291	18 828	20 666	22 795	28 352	124	13,6
EUR 10	44 393	50 834	59 691	74 272	86 715	106 568	120 542	127 523	141 809	158 013	111	15,1
España	594	735	934	1 321	1 586	2 150	2 298	2 628	3 513	3 922	112	23,0
Portugal	97	135	206	245	206	206	262	259	313	443	142	18,4
Sverige	3 006	3 273	4 027	5 097	6 115	7 237	7 295	7 268	8 265	8 829	107	12,7
USA	18 578	19 367	23 573	32 321	37 220	49 542	44 042	46 511	51 365	59 476	116	13,8
Nippon (Japan)	10 104	12 172	15 257	21 159	22 087	35 920	39 228	43 604	40 362	54 491	135	21,0

Source: 'Eurostat Review 1971-80', EEC Statistical Office, Brussels/Luxembourg, Nov. 1981.

Tables 16 and 17 show trends in import penetration and export/sales ratios in the UK mechanical engineering industries. Ratio 1 (imports/home demand) shows the share of imports in the home market. However, this ratio takes no account of the domestic industry's involvement in export markets which may compensate for the level of imports. Ratio 2 allows for this by reducing as exports increase. Similarly, Ratio 3 (exports/manufacturer' sales) makes no allowance for the degree of import penetration of the domestic market, and Ratio 4 makes the parallel adjustment.

The tables reveal that high export/sales ratios are positively associated with high import rations in mechanical engineering. This apparent anomaly has two possible explanations: either a) firms which are geared to exports are unable to respond to the demands of the domestic market[1]; or b) the products which are exported differ from those which are imported. The tables also suggest that import penetration in UK mechanical engineering is growing more rapidly than exports/sales, although both have increased over the last decade.

These figures may, however, be misleading to a certain extent because they do not take account of changes in the volume of industrial production in mechanical engineering. An increase in the exports/sales ratio, for example, may be due not so much to a rise in the real level of exports themselves as to a fall in domestic production.

Although at first sight it appears that export performance has improved, an analysis of Ratios 1-4 together with Table 19 clearly indicates that in absolute terms exports have been falling. Any improvement in the exports/sales figures thus does indeed reflect a deterioration in domestic production rather than an increase in exports. There has been no question of diverting resources from home to export markets or of an export-led recovery. Meanwhile, the UK domestic position has been a falling share of a falling market.

---

1 This point is made by C.Saunders, p.40

TABLE 16

IMPORT PENETRATION RATIOS, PER CENT

Notes

1. Standard industrial classification
2. Weight per 1,000 used in the Index of Industrial Production - base year 1975.

SIC[1] Order VII Mechanical Eng. MLH		Output Weight[2]	Ratio 1: Imports / Home Demand											Ratio 2: Imports / Home Demand + Exports									
			1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979
331	Agricultural Machinery (except tractors)	2	22	21	28	34	41	41	44	44	44	47	48	14	15	19	23	28	27	30	29	29	32
332	Metal Working Machine Tools	5	28	28	34	35	43	42	45	43	47	47	48	20	18	22	25	29	27	29	28	31	34
333	Pumps, Valves & Compressors	9	17	22	20	23	23	27	30	29	27	28	30	12	15	14	16	16	17	19	19	18	19
334	Industrial Engines	3	15	14	20	23	26	26	21	23	24	37	36	9	8	11	12	14	14	12	13	13	17
335	Textile Machinery & Accessories	3	48	51	53	57	64	62	73	56	58	61	76	22	21	22	27	27	23	26	27	29	29
336	Construction & Earth-Moving Equipment	5	40	37	31	37	49	59	58	63	69	59	72	20	16	16	21	23	22	23	22	24	25
337	Mechanical Handling Equipment	6	12	14	16	17	22	22	23	23	24	25	26	9	10	12	13	16	15	15	16	17	18
338	Office Machinery	2	51	51	52	66	69	69	84	91	110	100	120	34	30	32	41	41	40	48	47	54	56
339	Other Machinery	19	21	22	29	32	34	32	33	33	35	37		15	15	19	22	23	20	21	22	23	25
341	Industrial Plant & Steelwork	22	4	6	7	7	8	10	10	9	10	10		4	5	5	6	7	8	7	6	7	7
349	Other Mechanical Eng.	14	8	9	11	14	16	16	17	17	16	14		7	7	9	10	12	12	13	14	13	12
	Total (excl. MLH 341.3 and 349)	90	19	19	22	26	28	27	29	29	31	32	32	14	13	15	18	19	18	19	19	20	21

Source: Business Monitor MQ12 'Import Penetration and Export Sales Ratios for Manufacturing Industry'

TABLE 17

EXPORT SALES RATIOS, PER CENT

SIC[1] Order VII Mechanical Eng.

MLH		Output Weight[2]	Ratio 3: Exports / Manufacturers' Sales											Ratio 4: Exports / Manufacturers' Sales + Imports									
			1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979
331	Agricultural Machinery (except tractors)	2	42	36	40	40	43	46	44	49	47	45	49	36	31	33	30	31	33	31	35	34	30
332	Metal Working Machine Tools	5	36	43	44	40	46	50	50	50	48	43	50	29	35	34	30	32	36	35	36	33	29
333	Pumps, Valves & Compressors	9	32	35	39	37	39	45	46	44	43	39	48	28	30	34	31	33	37	37	36	35	32
334	Industrial Engines	3	46	48	51	53	52	52	48	48	52	66	69	42	44	45	46	45	44	42	41	45	55
335	Textile Machinery & Accessories	3	69	74	76	72	79	81	87	71	70	73	88	54	59	59	52	57	63	64	52	50	52
336	Construction & Earth-Moving Equipment	5	62	66	58	56	69	81	78	84	86	77	89	50	56	49	44	53	63	61	66	65	58
337	Mechanical Handling Equipment	6	27	33	27	26	31	36	38	40	35	33	37	25	30	24	22	26	30	33	33	29	27
338	Office Machinery	2	49	58	56	64	70	71	82	91	111	100	123	32	41	38	38	41	43	42	49	51	44
339	Other Machinery	19	34	37	40	37	42	45	46	43	43	44		29	31	32	29	33	36	36	34	33	33
341	Industrial Plant & Steelwork	22	16	19	22	18	18	23	28	31	32	30		15	19	20	17	17	21	26	29	30	28
349	Other Mechanical Eng.	14	16	21	25	27	27	27	27	25	24	18		17	20	23	24	24	23	24	22	21	16
	Total (excl. MLH 341.3 and 342)	90	33	37	38	36	40	43	45	44	44	42	46	29	32	32	30	32	35	36	36	35	33

Notes

1. Standard industrial classification.
2. Weight per 1,000 used in the Index of Industrial Production

Source: Business Monitor MQ12 'Import Penetration and Export Sales Ratios for Manufacturing Industry'.

Table 18 Trade in mechanical engineering products £ million

IMPORTS (c.i.f.)

MLH		1975	1976	1977	1978	1979	1980
331	Agricultural machinery (except tractors)	70.2	99.1	111.4	121.8	142.9	127.2
332	Metal-working machine tools	165.9	205.3	222.4	319.0	407.0	403.0
333	Pumps, valves & compressors	137.2	186.0	227.5	249.2	288.5	279.6
334	Industrial engines	63.4	58.6	78.2	86.5	95.2	98.2
335	Textile machinery	82.1	95.0	98.2	114.0	120.7	104.3
336	Construction & earth-moving equipment	161.3	216.1	238.1	274.5	314.7	283.5
337	Mechanical handling equipment	120.7	133.9	175.8	217.7	249.4	263.1
	Total Mechanical Engineering (SIC Order VII)	1601.4	1945.8	2261.1	2812.9	3377.3	3414.7
	MLH 331-337 as % of total	50	51	51	49	48	46

EXPORTS (f.o.b.)

MLH		1975	1976	1977	1978	1979	1980
331	Agricultural machinery (except tractors)	85.3	99.9	135.7	141.2	133.7	129.5
332	Metal-working machine tools	227.9	248.5	288.2	339.6	344.5	427.7
333	Pumps, valves & compressors	293.7	374.5	435.4	494.6	478.6	601.6
334	Industrial engines	188.3	197.6	244.7	292.5	312.2	390.4
335	Textile machinery	223.7	234.8	187.5	200.0	215.1	241.6
336	Construction & earth-moving equipment	470.6	574.9	718.8	741.9	734.1	848.4
337	Mechanical handling equipment	241.4	286.3	374.9	365.1	371.3	460.4
	Total Mechanical Engineering (SIC Order VII)	3181.3	3767.8	4402.5	5109.8	5311.7	6142.7
	MLH 331-337 as % of total	54	54	54	50	49	50

Source: derived from 'Business Monitor MQ10: Overseas Trade Analysed in Terms of Industries'.

Table 19

Index numbers of industrial production at constant factor cost
1975 = 100

	Weight per 1000	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981
Mining and quarrying	*41*	119·2	100·3	110·3	89·7	100·0	127·9	193·5	241·1	307·3	312·9	332·4
Manufacturing:												
Food, drink and tobacco	*77*	95·0	99·0	103·1	102·5	100·0	102·5	104·0	106·2	107·6	106·6	104·1
Coal and petroleum products	*9*	113·3	112·4	120·6	116·0	100·0	105·7	102·7	101·4	105·3	93·3	85·6
Chemicals and allied industries	*57*	89·1	94·3	105·3	109·5	100·0	112·0	115·9	117·0	119·3	109·9	108·6
Metal manufacture	*47*	115·3	115·4	126·3	115·5	100·0	104·9	104·4	103·4	104·6	74·7	78·6
Mechanical engineering	*92*	92·9	89·3	97·1	101·2	100·0	95·4	94·0	92·4	91·4	85·8	76·9
Instrument engineering	*12*	86·8	85·6	92·4	98·7	100·0	97·7	100·1	106·2	109·5	107·8	100·5
Electrical engineering	*66*	84·8	89·0	101·2	104·5	100·0	98·1	102·0	107·9	113·5	114·3	108·8
Shipbuilding and marine engineering	*14*	103·9	94·2	95·4	98·9	100·0	96·5	93·5	86·4	78·1	69·2	68·5
Vehicles	*68*	105·5	109·5	113·3	108·9	100·0	99·2	101·6	102·0	99·0	94·1	85·4
Metal goods not elsewhere specified	*46*	100·1	102·3	110·4	109·1	100·0	99·0	103·8	102·2	98·5	83·6	73·3
Textiles	*40*	108·0	110·4	116·5	105·8	100·0	102·8	100·8	99·0	96·0	79·3	71·3
Leather, leather goods and fur	*3*	108·8	110·4	107·1	98·7	100·0	102·4	97·1	97·3	92·3	72·3	65·5
Clothing and footwear	*24*	93·9	96·0	102·1	100·2	100·0	97·1	103·2	105·6	107·5	93·7	84·7
Bricks, pottery, glass, cement, etc.	*28*	97·3	104·0	113·6	107·2	100·0	100·6	99·6	101·4	100·9	90·8	83·0
Timber, furniture, etc.	*25*	93·4	102·9	120·2	102·3	100·0	103·3	96·8	101·3	102·8	88·9	80·8
Paper, printing and publishing	*58*	100·0	105·6	115·2	115·2	100·0	102·4	106·7	109·1	112·4	105·4	99·9
Other manufacturing industries	*31*	94·4	98·6	110·3	106·8	100·0	108·7	114·7	118·0	117·9	107·5	96·2
Total manufacturing	*697*	97·5	100·0	108·4	106·6	100·0	101·4	103·0	104·0	104·4	95·5	89·6
Construction	*182*	112·9	115·0	117·8	105·6	100·0	98·6	98·2	104·9	101·3	95·9	84·9
Gas, electricity and water	*80*	86·7	93·0	98·6	98·5	100·0	102·3	106·4	109·7	116·1	113·0	112·9
Total industrial production	*1000*	99·7	101·9	109·4	105·1	100·0	102·1	106·1	110·3	113·1	105·9	100·6
Other than extraction of mineral oil and natural gas (MLH 104)	*999·7*	*99·6*	*101·7*	*109·2*	*105·1*	*100·0*	*100·7*	*101·9*	*104·1*	*104·3*	*96·9*	*90·6*

Source: Central Statistical Office,
'National Income and Expenditure', 1982.

Growth in exports in the first half of the decade was aided by a depreciation in sterling after it was floated in 1972, making UK exports relatively more competitive on world markets.[1] At the same time, rising UK prices[2] and growth of the home market[3] resulted in an increase in import penetration.

Falling markets had an adverse effect on production levels from 1975. UK exports suffered a loss in competitiveness as a result of both domestic inflation[4] and the appreciation of sterling between 1977 and 1980.[5] The fact that imports have maintained their absolute market share may be due to the fact that imported products are not as affected by domestic cost inflation as domestic products and may thus more easily remain competitive, and also because the appreciation of sterling gave imports more price flexibility.

Table 20 Trade Conversion Factors (exports)

Units of national currency per £ sterling

	W.Germany D-mark	France franc	Italy lira	Japan yen	USA dollar
1970	8.784	13.333	1500	863.3	2.40000
1973	6.480	10.864	1434	666.2	2.45159
1974	6.044	11.250	1521	683.0	2.34254
1975	5.441	9.470	1447	657.1	2.21439
1976	4.509	8.580	1496	532.6	1.79501
1977	4.047	8.577	1545	469.5	1.74637
1978	3.839	8.646	1627	404.1	1.91949
1979	3.893	9.038	1758	465.4	2.12669
1980	4.223	9.834	2005	526.2	2.32577

Source: Based on trade conversion factors in United Nations Yearbook of International Trade Statistics, 1980.

Trade Conversion Factors represent exchange rates (annual averages) used by the United Nations for conversion of trade statistics.

1 See Tables 20 and 21
2 See Table 22. See also Table 23 for relative price performance.
3 See Table 19.
4 See Table 22.
5 See Tables 20 and 21.

Table 21 Exchange Rates

a) Effective Exchange Rate Index[1]
1975 = 100

	UK	W.Germany	France	Italy	Japan	USA
1976	85.6	104.8	95.6	82.3	104.2	105.2
1977	81.2	113.0	91.3	75.5	115.2	104.7
1978	81.5	120.1	91.3	71.1	141.7	95.7
1979	87.2	127.5	93.4	69.4	131.5	93.7
1980	96.1	128.8	94.4	67.2	126.5	93.9
1981	94.9	119.3	84.4	58.3	142.9	105.7
1982	90.5	124.3	76.7	53.9	134.8	118.1

b) Dollar Rate Index
1975 = 100

	UK	W.Germany	France	Italy	Japan
1976	81.3	97.6	89.7	78.7	100.1
1977	78.6	105.8	87.1	73.9	110.8
1978	86.4	122.4	95.0	76.9	142.3
1979	95.5	134.0	100.7	78.5	135.9
1980	104.7	135.3	101.4	76.3	131.4
1981	91.3	109.0	79.2	57.8	134.9
1982	78.8	101.3	65.5	48.4	119.5

1 The effective exchange rate is an index combining the currency in question with the other major currencies, weighted by the estimated effect on the trade balance of the country in question of a 1% change in the domestic currency price of one of the other currencies.

Source: International Monetary Fund, 'International Financial Statistics'.

Table 22 Wholesale Prices Indices for Mechanical Engineering (SIC Order VII) Annual averages 1975 = 100

	Output of manufactured goods (home sales)	Materials purchased by manufacturing industry
1974	79.3	79.2
1975	100.0	100.0
1976	117.6	121.0
1977	136.7	140.2
1978	152.8	153.9
1979	171.1	171.3
1980	194.5	189.1
1981	210.2	198.8

Source: Annual Abstract of Statistics, 1983.

- Price performance

Between 1975[1] and October 1982,[2] the unit value of UK exported non-electrical machinery, as evidenced by Table 23, rose by 132%. This was substantially more than the percentage increases for her three strongest competitors in this product area, namely the USA, West Germany and Japan. The UK increase has, however, over this period been diluted on foreign markets by exchange rate movements.

Between 1975 and 1978, during which time sterling was depreciating against the deutschemark, the effect of a weakening exchange rate was to reduce the sterling price increase of 68% to only 18% in deutschemark terms. While this rate of increase was still higher than those of the UK's competitors, the uncompetitiveness of British engineering exports was thus greatly shielded. Between 1978 and 1981, however, the strengthening of sterling not only exposed this uncompetitiveness but contributed towards it. With sterling appreciating by 15.4% against the deutschemark, the unit value of UK exported non-electrical machinery rose by 43.4% in D-mark terms over this period. A weakening of sterling between 1981 and October 1982 contributed significantly towards the slowing down of this rate of increase.

1 Equalisation of export price indices at a single level.
2 Latest available statistics.

Table 23 International Comparisons of Export Prices

	1974	1975	1976	1977	1978	1979	1980	1981	Oct. 1982
UK									
Unit value index of exported non-electrical machinery (1975 = 100)	79	100	121	148	168	179	199	215	232
Exchange rate (£ per DM)	0.165	0.183	0.220	0.247	0.260	0.257	0.237	0.220	0.233
Index expressed in DM(1975 = 100)	87	100	101	110	118	127	153	179	182
USA									
Unit value index of exported non-electrical machinery (1975 = 100)	88	100	107	114	123	134	150	167	182
Exchange rate ($ per DM)	0.386	0.406	0.397	0.430	0.499	0.547	0.551	0.444	0.397
Index expressed in DM(1975 = 100)	93	100	109	108	100	99	111	153	186
WEST GERMANY									
Unit value index of exported non-electrical machinery (1975 = 100)	92	100	104	110	112	116	122	127	135
JAPAN									
Unit value index of exported non-electrical machinery (1975 = 100)	98	100	98	97	92	98	102	102	107
Exchange rate (Yen per DM)	112.5	120.6	117.8	115.6	104.6	119.8	124.3	97.5	106.8
Index expressed in DM(1975 = 100)	106	100	100	101	106	99	99	126	121

Source: Engineering Employers Federation, 'Mechanical Engineering Short Term Trends" reports.

On the whole over the 1975-82 period, weak sterling had a beneficial effect on UK competitiveness in this product area. It reduced a 132% rise in the sterling price of UK exports to 82% in D-mark terms. Thus although the dollar price of US exports rose by 82% during this time, the rapid appreciation of the dollar against the deutschemark between 1980 and 1982 meant that by October 1982 US prices had increased by a greater proportion than UK prices in deutschemark terms. Similarly, as the Japanese yen strengthened against the deutschemark between 1980 and 1982 (and particularly between 1980 and 1981), this pushed up the D-mark price of Japanese exported non-electrical machinery to 21% above the 1975 level by October 1982.

Taking exchange rate movements into account, then, UK export unit values in this product area rose between 1975 and 1982 by 34.8% relative to West German export values and by 50.4% relative to Japanese prices, but fell by 2.15% against US prices.

While a further depreciation of sterling would have a beneficial effect on deutschemark prices of UK exports, it should be stressed that exchange rates are only one component of export prices. The uncompetitive behaviour of UK prices relative to West German and Japanese prices between 1975 and 1982 was due not to exchange rates but to inflation rates above those of West Germany and Japan of the non-exchange rate factors in export prices. The favourable performance of UK export prices relative to US export prices over this period was due to the strength of the dollar between 1980 and 1982.

- Market shares

Table 25 shows that percentage shares of mechanical engineering exports by selected market economies in 1980 as follows; W.Germany 22.7%, USA 22.3%, UK 11.6%, Japan 11.1%, France 8.3%; and Italy 8.1%.

This represents an improvement by the UK on 1975, for which year the following percentage shares of OECD exports of mechanical engineering were given by Saunders[1]:

---

1 C.Saunders, p.52

W.Germany 24.4%; UK 9.8%; France 8.4%.

This would mean that UK exports fell more slowly than world markets over this period.

The improvement was not in mechanical engineering alone, however. The following table shows that the UK share of total exports by these developed market economies recovered in 1980 after falling in the first half of the 1970s:

Table 24 Percentage shares of total exports of developed market economies.

	1970	1975	1980
UK	8.60	7.62	9.08
W. Germany	15.20	15.56	15.19
France	7.97	9.02	8.76
Italy	5.87	6.02	6.11
USA	18.94	18.35	17.06
Japan	8.59	9.65	10.17

Source: derived from United Nations Yearbook of International Trade Statistics, 1980.

- Unit values

Table 27 shows that the average export unit value of UK mechanical engineering products is below that of West German products, but above those of France, Italy and Japan. This does not mean, however, that UK products are more competitive than their West German counterparts. Price is only one element of competitiveness, which depends also on factors such as speed of delivery, servicing, reliability and quality. Given that these statistics are of actual sales (so that they exclude instances where products have been priced out of the market), a significant difference in price implies either a difference in composition of the categories between the countries concerned or differences in non-price factors, such as quality.

The fact that UK import unit values are higher than her export unit values certainly implies that UK imports of mechanical engineering products are of a higher quality than her exports. If this were not the case, UK exporters would instead seek to sell their products on the home market at a higher price than they could obtain abroad.

In only six of the twenty two product groups in Tables 25-27 was the UK export price higher than the West German, implying that West German quality is consistently higher, and her products at a more sophisticated end of the range, than that of the UK. These figures confirm similar results obtained by Saunders.[1] However, in only seven instances was the French export price higher than the UK export price, and in only three cases was the Italian export price higher than the UK export price.

From the data, it would appear that Japan imports a small amount (Japan imports significantly less mechanical engineering equipment than the UK, France or West Germany) of very expensive, high technology equipment, and exports much cheaper products.

Differences in export unit values may of course reflect not just differences in quality, but also uncompetitive pricing - though not sufficiently so that goods are priced out of the market. It has already been shown that absolute export levels in UK mechanical engineering fell in real terms between 1975 and 1980. This may reflect both falling world markets and uncompetitive pricing resulting in a fall in demand for UK products.

The problem with unit values is that they reflect the prices of actual sales, and do not therefore include products which have been priced out of the market. Thus they are of little use in competitive markets in which producers face a world price, although they may be of use in imperfectly competitive markets, in which competing products are sufficiently different to allow their prices to vary, but sufficiently similar for the price to affect the volume of sales, so that exporters face a smoothly downward-sloping demand curve.

---

1 C.Saunders, chapter 4.

Table 25 Exports of mechanical engineering products, 1980.

SITC[1]		UK		W.GERMANY		FRANCE		ITALY		USA[4]	JAPAN	
		Volume[2]	Value[3]	Volume	Value	Volume	Value	Volume	.Value	Value	Volume	Value
711	Steam Boilers & Aux. Plant	23867	134980 (8.47)[5]	46440	291851 (18.31)	15783	93626 (5.87)	24994	128977 (8.09)	312172 (19.58)	85715	353171 (22.16)
712	Steam Engines, Turbines	8722	160072 (11.12)	12720	260368 (18.10)	8269	172765 (12.01)	5412	63933 (4.44)	276827 (19.24)	17745	204413 (14.21)
713	Internal Combustion Piston Engines	223419	1833293 (12.41)	322339	2874999 (19.45)	151808	1231166 (8.33)	93645	709489 (4.80)	3716990 (25.15)	308192	1782899 (12.06)
714	Engines and Motors NES	27929	2296049 (30.53)	6647	382574 (5.09)	6503	280262 (3.73)	5009	251151 (3.34)	2714280 (36.09)	7588	109887 (1.46)
716	Rotating Electric Plant	85393	679208 (10.68)	124069	1218305 (19.15)	70582	662675 (10.42)	40746	299848 (4.71)	1188690 (18.69)	..	917549 (14.42)
718	Other Power Generating Machinery	..	89895 (4.72)	10872	275610 (14.49)	12399	275870 (14.50)	3571	30639 (1.61)	472626 (24.84)	12624	97746 (5.14)
721	Agricultural Machinery, excluding Tractors	62393	332626 (6.30)	186278	888856 (16.84)	92127	390979 (7.41)	75935	322908 (6.12)	1300148 (24.64)	21550	141584 (2.68)
722	Tractors Non-Road	247367	1077271 (16.89)	212303	950325 (14.90)	50185	229107 (3.59)	174064	755463 (11.84)	1828427 (28.66)	212502	781028 (12.24)

Table 25 cont'd.

SITC		UK		W.GERMANY		FRANCE		ITALY		USA	JAPAN	
		Volume	Value	Volume	Value	Volume	Value	Volume	Value	Value	Volume	Value
723	Civil Engineering Equip.,etc.	298654	1614254 (11.36)	327836	1620234 (11.41)	264586	1306025 (9.19)	101297	424453 (2.99)	5169308 (36.39)	464634	1315006 (9.26)
724	Textile, Leather Machinery	55332	697732 (7.37)	175211	2636677 (27.84)	41041	488663 (5.16)	94687	932306 (9.84)	726839 (7.67)	..	1344261 (14.19)
725	Paper etc. Mill. Machinery	28805	228818 (8.93)	53403	683167 (26.66)	13540	146943 (5.73)	18391	164251 (6.41)	314987 (12.29)	10598	92725 (3.62)
726	Printing, Bookbinding Machinery & parts	23515	413622 (11.73)	79294	1329016 (37.69)	8390	138751 (3.94)	13247	176338 (5.00)	686603 (19.47)	16052	184354 (5.23)
727	Food Machinery, Non-Domestic	18485	222733 (10.67)	27733	434736 (20.83)	21126	182705 (8.75)	18439	200408 (9.60)	337032 (16.15)	4261	39963 (1.91)
728	Other Machinery for Specialised Industries	134490	1398595 (9.42)	391679	3818097 (25.71)	114524	1074343 (7.23)	232768	1691894 (11.39)	2296453 (15.46)	152192	1178869 (7.94)
736	Metalworking Machine Tools	98073	867404 (7.74)	232814	3287862 (29.34)	56480	660016 (5.89)	106524	972612 (8.68)	1275028 (11.38)	161043	1567986 (13.99)
737	Metalworking Machinery NES	58822	259368 (8.12)	179204	740407 (23.19)	38687	241240 (7.55)	64243	284434 (8.91)	552241 (17.29)	91541	289250 (9.06)

Table 25 cont'd.

SITC		UK Volume	UK Value	W.GERMANY Volume	W.GERMANY Value	FRANCE Volume	FRANCE Value	ITALY Volume	ITALY Value	USA Value	JAPAN Volume	JAPAN Value
741	Heating, Cooling Equipment	90480	832682 (7.46)	180889	1756202 (15.73)	145738	979314 (8.77)	211215	1187249 (10.63)	2344202 (20.99)	..	1685433 (15.09)
742	Pumps for Liquids, etc.	40415	594608 (10.78)	79237	1292352 (23.43)	37979	516578 (9.37)	44172	389143 (7.06)	1044996 (18.95)	51151	439504 (7.97)
743	Pumps NES, Centrifuges, etc.	80166	842034 (9.91)	160139	1698142 (19.98)	88778	815485 (9.59)	112976	732779 (8.62)	1753101 (20.62)	124189	779899 (9.17)
744	Mechanical Handling Equipment	190479	1091225 (9.55)	309323	1989820 (17.42)	216578	1065892 (9.33)	142576	622575 (5.45)	2557252 (22.39)	422527	1312643 (11.49)
745	Non-electric machinery, tools NES	35240	521186 (7.46)	112427	2029340 (29.06)	24526	306443 (4.39)	42098	616355 (8.82)	1300017 (18.61)	34362	423993 (6.07)
749	Non-electric mach. parts, accessories NES	153528	1518271 (9.57)	396835	4074372 (25.68)	153681	1450306 (9.14)	188000	1441350 (9.08)	1822334 (11.49)	282273	1834844 (11.56)
	TOTAL	1985574	17705926 (11.6%)	3627692	34533312 (22.7%)	1633310	12709154 (8.3%)	1813919	12398555 (8.1%)	33990613 (22.3%)	2480739[6]	16877007 (11.1%)

1 Group (3-digit) level of the Standard Industrial Trade Classification, Revision 2.
2 Metric Tons
3 Thousands of US dollars
4 No volume data available
5 Figures in brackets show % share of total exports by market economies.
6 Excluding SITC 716, 724, 741.

Source: United Nations Yearbook of International Trade Statistics 1980.

Table 26 Imports of mechanical engineering products, 1980.

SITC[1]		UK		W.GERMANY		FRANCE		ITALY		JAPAN	
		Volume[2]	Value[3]	Volume	Value	Volume	Value	Volume	Value	Volume	Value
711	Steam Boilers & Aux. Plant			4346	18972						
712	Steam Engines, Turbines	1761	23974	2548	28594	4563	47423	617	16389		
713	Internal Combustion Piston Engines	115908	632118	117760	825133	143931	1017033	95857	749002		
714	Engines and Motors NES	6177	1292423	3368	428132	3052	543484	1236	237397	1564	333530
716	Rotating Electric Plant	23670	238953	87593	528292	44907	333362	61806	298180	8309	118864
718	Other Power Generating Machinery	1652	32773	6101	84093	4272	285966	1360	24107	795	44509
721	Agricultural Machinery, excluding Tractors	65899	315620	81418	341750	134625	573985	37042	176811	14483	78180
722	Tractors Non-Road	35384	163271	33101	148857	104556	450532	36292	146317		
723	Civil Engineering Equipment, etc.	111364	521393	168060	687024	163361	742684	91759	400211		
724	Textile, Leather Machinery	33802	410893	46338	486341	38343	496680	40556	570989		
725	Paper etc. Mill. Machinery	13021	159240	23508	211069	14596	150559	8626	108585	2923	44112
726	Printing, Bookbinding Machinery & parts	22241	373417	15147	219901	18284	304326	13621	191744	7916	138105
727	Food Machinery, Non-Domestic	7487	113711	8615	93832	8269	109412	4095	52824		
728	Other Machinery for Specialised Industries	62967	743172	99986	916283	99828	890839	32333	389484	18976	332190

Table 26 cont'd.

SITC		UK		W.GERMANY		FRANCE		ITALY		JAPAN	
		Volume	Value	Volume	Value	Volume	Value	Volume	Value	Volume	Value
736	Metalworking Machine Tools	64424	779988	95357	972613	64406	706533	54269	432540	18764	258872
737	Metalworking Machinery NES	20841	169019	46151	223672	60624	171300	32771	116585		
741	Heating, Cooling Equipment	57427	471430	84920	661579	76416	599481	21944	204513	..	177382
742	Pumps for Liquids, etc.	19979	281687	41703	381813	32187	417657	17700	272331	4607	100542
743	Pumps NES, Centrifuges, etc.	41068	429174	86253	642173	85881	709969	36225	332439	17821	206758
744	Mechanical Handling Equipment	119765	622157	167680	636021	142390	734154	70193	325900		
745	Non-electric machinery, tools NES	28392	473612	38797	494366	36680	600490	15041	244294	5920	152725
749	Non-electric machine parts, accessories NES	92574	1006203	185342	1564286	147063	1388556	82161	880992	14925	297805
	TOTAL	945803	9254228	1444092	10594796	1428234	11274425	755504	6171634	117003[4]	2283574

1 Group (3-digit) level of the Standard International Trade Classification, Revision 2.
2 Metric Tons
3 Thousands of US dollars
4 Excluding SITC 741.

Source: United Nations Yearbook of International Trade Statistics 1980.

Table 27. Export and Import Unit Values of Mechanical Engineering Products, (thousands of US dollars per metric ton)

1980.

SITC[1]		UK		W.GERMANY		FRANCE		ITALY		JAPAN	
		Export Unit Value	Import Unit Value	Export Unit Value	Import Unit Value	Export Unit Value	Import Unit Value	Export Unit Value	Import Unit Value	Export Unit Value	Import Unit Value
711	Steam Boilers & Aux. Plant	5.66	-	6.28	4.37	5.93	-	5.16	-	4.12	-
712	Steam Engines, Turbines	18.35	13,61	20.47	11.22	20.89	10.39	11.81	26.56	11.52	-
713	Internal Combustion Piston Engines	8.21	5.45	8.92	7.01	8,11	7.07	7.58	7.81	5.79	-
714	Engines & Motors NES	82.21	209.23	57.56	127.11	43.10	178.07	50.14	192.07	14.48	213.25
716	Rotating Electric Plant	7.95	10.10	9.82	6.03	9.39	7.42	7.36	4.82	-	14.31
718	Other Power Generating Machinery	-	19.84	25.35	13.78	22.25	66.94	8.58	17.73	7.74	55.99
721	Agricultural Machinery, excluding Tractors	5.33	4.79	4.77	4.20	4.24	4.26	4.25	4.77	6.57	5.40
722	Tractors, Non-Road	4.35	4.61	4.48	4.50	4.57	4.31	4.34	4.03	3.68	-
723	Civil Engineering Equipment, etc.	5.41	4.68	4.94	4.09	4.94	4.55	4.19	4.36	2.83	-
724	Textile, Leather Machinery	12.61	12.16	15.05	10.50	11.91	12.95	9.85	14.08	-	-
725	Paper etc. Mill. Machinery	7.94	12.23	12.79	8,98	10.85	10.32	8.93	12.59	8.75	15.09
726	Printing, Bookbinding Machinery & Parts	17.59	16.79	16.76	14.52	16.54	16.64	13.31	14.08	11.48	17.45
727	Food Machinery, Non-Domestic	12.05	15.19	15.68	10.89	8.65	13.23	10.87	12.90	9.38	-
728	Other Machinery for Specialised Industries	10.40	11.80	9.75	9.16	9.38	8.92	7.27	12.05	7.75	17.51

Table 27 cont'd.

SITC		UK		W.GERMANY		FRANCE		ITALY		JAPAN	
		Export Unit Value	Import Unit Value	Export Unit Value	Import Unit Value	Export Unit Value	Import Unit Value	Export Unit Value	Import Unit Value	Export Unit Value	Import Unit Value
736	Metalworking Machine Tools	8.84	12.10	14.12	10.20	11.69	10.97	9.13	7.97	9.74	13.80
737	Metalworking Machinery NES	4.41	8.11	4.13	4.85	6.24	2.83	4.43	3.56	3.16	-
741	Heating, Cooling Equipment	9.20	8.21	9.71	7.79	6.72	7.84	5.62	9.32	-	-
742	Pumps for Liquids, etc.	14.71	14.10	16.31	9.16	13.60	12.98	8.81	15.39	8.59	21.82
743	Pumps NES, Centrifuges, etc.	10.50	10.45	10.60	7.45	9.19	8.27	6.49	9.18	6.28	11.60
744	Mechanical Handling Equipment	5.73	5.19	6.43	3.79	4.92	5.16	4.37	4.64	3.11	-
745	Non-electric machinery, tools NES	14.79	16.68	18.05	12.74	12.49	16.37	14.64	16.24	12.34	25.80
749	Non-electric machine parts, accessories NES	9.89	10.87	10.27	8.44	9.44	9.44	7.67	10.72	6.50	19.95
	AVERAGE	8.87[2]	9.77[2]	9.52	7.34	7.78	7.89	6.84	8.17	6.80[3]	18.28[3]

1 Group (3-digit) level of the Standard International Trade Classification, Revision 2.
2 Excluding SITC 718.
3 Excluding SITC 716, 724, 741.

Source: Derived from United Nations Yearbook of International Trade Statistics 1980.

Table 28 Ratios of Export Unit Values/Import Unit Values for Mechanical Engineering Products, 1980.

SITC[1]		UK	W.GERMANY	FRANCE	ITALY	JAPAN
711	Steam Boilers & Aux. Plant	-	1.44	-	-	-
712	Steam Engines, Turbines	1.35	1.82	2.01	0.44	-
713	Internal Combustion Piston Engines	1.51	1.27	1.15	0.97	-
714	Engines and Motors NES	0.39	0.45	0.24	0.26	0.07
716	Rotating Electric Plant	0.79	1.63	1.27	1.53	-
718	Other Power Generating Machinery	-	1.84	0.33	0.48	0.14
721	Agricultural Machinery, excluding Tractors	1.11	1.14	1.00	0.89	1.22
722	Tractors, Non-Road	0.94	1.00	1.06	1.08	-
723	Civil Engineering Equipment, etc.	1.16	1.21	1.09	0.96	-
724	Textile, Leather Machinery	1.04	1.43	0.92	0.70	-
725	Paper etc. Mill. Machinery	0.65	1.42	1.05	0.71	0.58
726	Printing, Bookbinding Machinery & parts	1.05	1.15	0.99	0.95	0.66
727	Food Machinery, Non-Domestic	0.79	1.44	0.65	0.84	-
728	Other Machinery for Specialised Industries	0.88	1.06	1.05	0.60	0.44
736	Metalworking Machine Tools	0.73	1.38	1.07	1.15	0.71
737	Metalworking Machinery NES	0.54	0.85	2.20	1.24	-
741	Heating, Cooling Equipment	1.12	1.25	0.86	0.60	-
742	Pumps for Liquids, etc.	1.04	1.78	1.05	0.57	0.39
743	Pumps NES, Centrifuges, etc.	1.00	1.42	1.11	0.71	0.54
744	Mechanical Handling Equipment	1.10	1.70	0.95	0.94	-
745	Non-electrical machinery, tools NES	0.89	1.42	0.76	0.90	0.48
749	Non-electric machine parts, accessories NES	0.91	1.22	1.00	0.72	0.33
	AVERAGE	0.91[2]	1.30	0.99	0.84	0.37[3]

1 Group (3-digit) level of the Standard International Trade Classification, Revision 2.
2 Excluding SITC 718.
3 Excluding SITC 716, 724, 741.

Source: Derived from United Nations Yearbook of International Trade Statistics 1980.

A Bank of England study[1] which considered various measures of competitiveness concluded that unit labour cost indices perform best at explaining the volume of manufactured exports, in particular using the IMF procedure to 'normalise' the index.[2] This index is displayed in Table 29.

From this table, it may be seen that although relative unit labour costs in the UK were reduced during the 'social contract' of 1975-77, since then increases in wage costs above that of productivity have resulted in the growth of unit wage costs being significantly greater in the UK than for her principal competitors, particularly since 1979. While relative normalised unit labour costs fell between 1975 and 1981 by 4.8% in W.Germany, 6.5% in France, 9.2% in Italy and 4.9% in Japan, and increased by 16.1% in the USA, they rose by 46.2% in the UK (and by 34.7% between 1979 and 1981 alone).

This means that where UK export prices are constrained by market conditions (i.e., where exporters are unwilling to sacrifice sales volume for price increases), a reduction in profit margins must follow. A clearing bank report[3] states that by the second half of 1980 it was widely believed that UK mechanical engineering companies were trading at little or no profit in overseas markets.

Table 29 Index of Relative Normalised Unit Labour Costs[1] (1975 = 100)

	1976	1977	1978	1979	1980	1981
UK	93.9	90.3	96.2	111.5	137.0	146.2
W.Germany	100.3	106.3	109.8	111.2	107.1	95.2
France	99.2	94.1	94.3	98.8	101.0	93.5
Italy	89.7	88.2	86.1	90.1	93.1	90.8
USA	105.8	105.4	97.8	96.4	98.9	116.1
Japan	97.4	102.9	115.8	99.4	87.3	95.1

[1] Vis-a-vis other industrial countries, as listed, Unit labour costs are defined as compensation of employees, per unit of real output (in the value added sense) in the manufacturing sector. Account is taken of employer-paid social insurance premia and other employment taxes as well as wages and salaries. The index is adjusted to eliminate estimated cyclical swings.

Source: International Monetary Fund, 'International Financial Statistics, April 1983.

1 C.A. Enoch, pp.181-96
2 This process adjusts for cyclical distortions caused by, for instance, labour hoarding during an economic downturn.
3 M.W.Henry.

2. Investment abroad

Table 30 shows expenditure on acquisitions of foreign companies by UK firms and vice-versa. The statistics are, however, limited in two important respects. First they are limited to acquisitions mentioned in the press; and secondly, only direct acquisitions are counted, so that acquisitions by existing foreign subsidiaries or associates are not included. This may substantially reduce the number of recorded acquisitions from the true totals.

The statistics record that between 1973, when Britain joined the Common Market, and 1981 UK firms directly acquired 171 companies within the EEC, but that in the same period only 38 UK firms were acquired by Community enterprises.

While allowing for the limitations of these statistics, the proportion by which the flows from the UK to the EEC outweighs the reverse flow is also indicated in Table 31, which shows that direct net investment by UK mechanical engineering firms and manufacturing industry in general in the EEC has on the whole consistently outweighed direct net investment in the UK by Community firms.

While these annual investment flows reflect additional direct investment, it may be argued that a more accurate indication of the presence of UK firms in the EEC, and Community enterprises in the UK, is given by the data on net earnings. The earnings figures do not relate directly to the investment figures for the corresponding years, as they reflect an earnings stream from existing operations and thus relate to investments in previous years.

The data show that the earnings of UK mechanical engineering subsidiaries in the EEC during the last decade were at their highest in 1976, when sterling was relatively weak. Earnings decreased over the next three years, during which time sterling was appreciating against the French franc and the Italian lira and later against the deutschemark, but they did recover somewhat in 1980.

Table 30a Expenditure on Acquisitions of Foreign Companies by UK Companies

	Total			EEC Countries		
	No. acquiring	No. acquired	£m	No. acquiring	No. acquired	£m
1971	53	62	73.0	19	20	26.5
1972	69	85	90.4	44	49	50.6
1973	80	88	178.5	53	57	73.7
1974	49	53	120.6	29	30	65.2
1975	17	18	41.3	9	10	29.9
1976	17	17	64.6	5	5	4.9
1977	18	18	142.8	6	6	8.2
1978	29	30	349.5	10	11	21.1
1979	55	63	344.8	10	11	46.6
1980	51	51	941.0	12	12	138.7
1981	139	150	726.2	25	29	23.6

Table 30b Expenditure on Acquisitions of UK Companies by Foreign Companies

	Total			EEC Countries		
	No. acquiring	No. acquired	£m	No. acquiring	No. acquired	£m
1971	19	21	32.7	2	2	0.5
1972	18	18	41.4	1	1	0.2
1973	5	8	58.0	1	1	9.0
1974	9	9	184.9	2	2	6.2
1975	9	9	53.5	3	3	4.7
1976	10	10	72.8	1	1	8.6
1977	12	12	79.5	3	3	1.3
1978	13	13	38.6	5	5	11.3
1979	6	6	47.1	3	3	6.1
1980	23	23	169.7	6	6	27.2
1981	72	75	493.4	12	14	36.3

Source: Business Statistics Office, 'Business Monitor MQ7: Acquisitions and mergers of industrial and commercial companies'.

Table 3/a Direct Net Investment and Earnings of UK firms in the EEC
£ million

	Net Investment[1]		Net Earnings[2]	
	Mechanical Engineering	Total Manufacturing	Mechanical Engineering	Total Manufacturing
1972	23.8	108.1	25.1	93.0
1973	17.8	272.5	33.7	188.3
1974	37.9	165.9	15.3	155.9
1975	-16.5 [3]	107.7	26.3	159.3
1976	24.0	286.1	45.4	277.4
1977	11.5	320.7	33.7	250.1
1978	18.9	301.7	8.5	268.1
1979	28.3	100.4	2.8	302.9
1980	26.5	121.9	15.3	179.7

Table 3/b Direct Net Investment and Earnings of EEC firms in the UK
£ million

	Net Investment[1]		Net Earnings[2]	
	Mechanical Engineering	Total Manufacturing	Mechanical Engineering	Total Manufacturing
1972	0.9	17.0	-1.4	33.5
1973	-1.6	28.8	-0.4	33.4
1974	1.6	28.3	-0.1	21.9
1975	7.8	33.2	4.5	17.2
1976	2.1	85.6	7.9	52.2
1977	4.7	108.7	7.1	94.2
1978	4.1	120.7	8.5	86.7
1979	18.2	105.7	10.4	62.9
1980	13.2	-93.3	8.8	-86.1

1 Direct net investment refers to investment, net of disinvestment, that adds to, deducts from, or acquires a lasting interest in an enterprise operating in an economy other than that of the investor, the investor's purpose being to have an effective voice in the management of the enterprise. Other investments in which the investor does not have an effective voice in the management of the enterprise are mainly portfolio investments and are not covered here.

2 Net earnings equal profits of overseas branches plus UK companies' receipts of interest from and their share of profits of overseas subsidiaries and associates. Earnings are after deducting provisions for depreciation and overseas tax on profits, dividends and interest.

3 A minus sign indicates net losses.

Source: Business Statistics Office, 'Business Monitor MA4: Overseas Transactions.

Earnings by UK subsidiaries of Community firms rose fairly steadily in the latter half of the decade, and in 1979 exceeded the flow of earnings to the UK mechanical engineering industry. This earnings growth was associated with a growth in net investment by EEC mechanical engineering firms in the UK.

Growing investment in the EEC by UK mechanical engineering firms towards the end of the decade, together with a weakening of sterling after 1980-81 may have resulted in a subsequent increase in UK earnings from the EEC.

3. Concentration

In 1979[1] there were 13,788 mecahnical engineering companies in the UK. Of these, however, 12,810 (93%) employed under 100 people. In all, these enterprises accounted for 20.7% of the sector's total employment, 18.2% of total sales and 25.0% of its net capital investment.

At the other end of the scale, 11.6% of employment, 12.0% of sales and 10.9% of capital expenditure were accounted for by only seven enterprises (and 16.4%, 16.7% and 15.8% respectively by the largest twelve enterprises).

Proponents of the view that efficiency increases with size through economies of scale would expect that productivity measured through gross value added per head would be highest in the largest enterprises. In actual fact this - at least in 1979 - was not so. Although productivity for this group was well above the average for the industry as a whole, the size group which yielded the highest productivity was the 1,500-1,999 employee range.

---

1 Latest available statistics.

Table 32 Analysis by size of total employment, 1979, SIC Order VII, Mechanical Engineering.

Size of enterprise (no. of employees)	No. of enterprises	No. of establishments	Employment (1000's)	Total sales + work done £ million	Net capital expenditure £ million	Gross value added per head at factor cost £
1- 99	12810	13295	183.1	2918.9	144.3	7673
100- 199	452	619	62.4	1164.6	47.9	
200- 499	263	484	81.2	1531.5	57.1	8020
500- 999	119	345	82.8	1671.9	51.3	8390
1000-1499	40	142	47.9	893.5	30.1	8605
1500-1999	29	123	50.9	936.6	23.6	9476
2000-2999	27	143	66.2	1203.4	38.2	7779
3000-3999	14	113	49.9	919.3	27.9	8387
4000-4999	10	100	45.6	975.9	27.8	8322
5000-7499	12	292	68.3	1144.0	38.3	8053
7500-9999	5	77	42.6	757.9	28.3	8640
10000 and over	7	99	102.6	1933.0	62.9	8784
TOTAL	13788	15832	883.5	16050.5	577.7	

Source: Business Statistics Office, 'Business Monitor PA 1002: Report on the Census of Production, Summary Tables, 1979' (1982)

Product concentration

Each Minimum List Heading (MLH) in the mechanical engineering (Standard Industrial Classification Order VII) sector can cover a number of different products. Concentration ratios at the MLH level may thus aggregate a number of different product markets yielding an average view which is not truly representative of the situation in each market. Prior to considering industry concentration ratios, then, it is first necessary to consider the relevant 'specialisation' indices; that is, the ratio of total sales of principal products by the industry concerned to total sales of goods produced and work done.

Trends in the indices of specialisation for the various branches of mechanical engineering between 1975 and 1979 are shown in Table 33.

Table 33 Index of Specialisation[1] by Industry, 1975-79[2], %.

MLH		1975	1976	1977	1978	1979
331	Agricultural machinery (excluding tractors)	82	88	90	82	77
332	Metal-working machine tools	93	93	95	94	93
333(1)	Pumps	84	87	85	85	85
333(2)	Valves	81	80	80	80	83
333(3)(4)	Compressors and fluid power equipment	77	82	88	87	86
334	Industrial engines	68	70	67	71	57
335	Textile machinery & accessories	91	89	88	91	90
336	Construction & earth-moving equipment	88	91	86	88	84
337	Mechanical handling equipment	92	90	94	93	92
338	Office machinery	80	74	70	77	77
339(1)	Mining machinery	85	86	86	86	87
339(2)	Printing, bookbinding & paper goods machinery	92	92	93	89	91
339(3)(4)	Refrigerating machinery, space-heating, ventilating and air-conditioning equipment	90	91	91	92	90
339(5)(6)	Scales & weighing machinery and portable power tools	85	87	89	91	87
339(7)(8)	Food & drink processing machinery and packaging & bottling machinery	75	77	74	73	78
339(9)	Miscellaneous (non-electrical) machinery	85	86	84	83	85
341	Industrial (including process) plant & steelwork	90	92	..	..	..
349(1)	Ball, roller, plain and other bearings	95	95	95	94	92
349(2)(3)	Precision chains and other mechanical engineering	85	86	87	85	85

1 The index of specialisation for an industry is the ratio of total sales of principal products by the industry to total sales of goods produced and work done.

2 Excludes MLH 342, Ordnance and small arms.

3 .. indicates that figures are not available.

Source: Census of Production 1979, Summary Tables (1982).

A high ratio indicates a fairly narrow product range, and a low one that products are diverse and that there are a number of different markets within the MLH.

The indices range from 57% for industrial engines, implying that a number of different products and therefore markets are included in this MLH, to 93% in the case of metal-working machine tools, so that the MLH is accounted for by a few principal products, with a little room for specialised products.

In most branches it can be seen that the great majority of sales are accounted for by the principal products.

Industry concentration[1]

Table 34 shows clearly that industrial concentration in mechanical engineering fell in almost every MLH between 1975 and 1979. This suggests a number of different possibilities:

a) New products have been introduced by smaller firms in branches in which the index of specialisation has fallen. It is also possible that the index of specialisation may have fallen as a result of demand for specialised products being more stable than that for the principal, mainstream products of the MLH.

b) Smaller firms have managed to become more cost competitive than larger firms in the face of falling demand and production; that is, they have pursued a policy of undercutting the large firms in order to survive, either by introducing efficiencies or by reducing their own profit margins.

c) Smaller firms have protected themselves against both the large firms and market conditions by producing specialised equipment which may have only a limited market and thus not appeal to the larger firms.

A problem with concentration ratios is that they do not take account of export and import ratios. Where these are high, concentration figures based on domestic production may be meaningless as far as the domestic market is concerned. It is certain that UK firms' domestic market shares have slipped as import penetration has increased (see pp.121-123).

1 See also pp. 198-202.

Table 34 Percentage shares of total sales accounted for by the largest five firms in each MLH[1] (1)

MLH		1975[2] %	1979[3] %	Index of production volume at constant prices, 1979 (1975 = 100)[4]
331	Agricultural machinery (excluding tractors)	46	31	86
332	Metal-working machine tools	29	26	81
333(1)	Pumps	39	29	101
333(2)	Valves	45	38	87
333(3)(4)	Compressors and fluid power equipment	41	32	100
334	Industrial engines	95	86	116
335	Textile machinery & accessories	58	47	36
336	Construction & earth-moving equipment	47	36	88
337	Mechanical handling equipment	30	24	85
338	Office machinery	59	55	76
339(1)	Mining machinery	55	57	118
339(2)	Printing, bookbinding & paper goods machinery	48	35	97
339(3)(4)	Refrigerating machinery, space-heating, ventilating and air-conditioning equipment	26	22	98
339(5)(6)	Scales & weighing machinery and portable power tools	77	74	127
339(7)(8)	Food & drink processing machinery and packaging & bottling machinery	50	39	68
339(9)	Miscellaneous (non-electrical) machinery	19	18	91
341	Industrial (including process) plant & steelwork	29	14	79
349(1)	Ball, roller, plain and other bearings	78	72	88
349(2)(3)	Precision chains and other mechanical engineering	29	17	97

1 Excludes MLH 342, Ordnance and small arms.

Sources: 2: 'Business Monitor PO 1006: Statistics of Product Concentration of UK Manufacturers 1975, 1976 & 1977', (1980);
3: 'Business Monitor PA 1002: Report on the Census of Production 1979, Summary Tables', (1982);
4: Engineering Employers Federation, 'Mechanical Engineering Short Term Trends Report', Nov.1982.

4. Profitability

It is not possible to provide figures for the standard measure of profitability, return on capital (trading profit/ capital employed), as there are no statistics available for capital employed in mechanical engineering. Table 35 contains other performance indicators.

Net profits, which discount the effect of depreciation, provide a more effective indication of profitability than gross profits. The figures show clearly that profits declined over the second half of the decade, which is to be expected given the fall in output, sales and gross value added. However, profitability - as distinct from absolute profit levels - has also declined, as evidenced by the fall in profit margins and in the ratio of profits to gross value added.

Full data since 1979 are not yet available; however, it is known that in nominal terms, gross profits in mechanical engineering fell in 1980 by 24% from the previous year, while net profits fell by 61%.[1] With wholesale prices rising by 13.7% during this year[2] and mechanical engineering production falling by 6.1%,[3] this fall in profits would have been even more significant in real terms.

Productivity measured in terms of real gross value added per employee fell by 9% between 1973 and 1977 and then increased by 4% in the next two years. Although real gross value added grew in 1979, the 1977-79 productivity increase was due largely to the fall in employment. Between December 1979 and July 1982,[4] employment in mechanical engineering fell to 693,000 - a fall of some 190,000 jobs, or 22%. Output volume per employee in in this sector was reported to have risen to 8% above its 1975 level by the second quarter of 1982, but again to have been due to reduced employment rather than increased output.[5]

---

1 National Income & Expenditure Accounts.
2 See Table 22.
3 See Table 19.
4 Latest available statistics.
5 Engineering Employers Federation, 'Mechanical Engineering Short Term Trends Report, November 1982.

Table 35 Performance indicators for the UK mechanical engineering sector, 1971-79.

		1971	1972	1973	1974	1975	1976	1977	1978	1979
Gross Output	£m	8847	8505	9247	9638	9524	9085	8952	8800	8705
Total Sales	£m	8657	8373	8850	8864	9195	8838	8676	8545	8542
Gross Value Added (GVA) at factor cost	£m	..	..	4201	4224	4205	4005	3886	3828	3862
Stocks	£m	525	463	449	470	512	566	569	568	550
Gross profits	£m	802	899	1005	951	853	848	833	860	864
Net profits	£m	460	524	598	526	443	479	460	449	413
Gross profit margin	%	9.3	10.7	11.4	10.7	9.3	9.6	9.6	10.1	10.1
Net profit margin	%	5.3	6.3	6.8	5.9	4.8	5.4	5.3	5.3	4.8
Gross profits / Gross Value Added	%	..	..	23.9	22.5	20.3	21.2	21.4	22.5	22.4
Net profits / Gross Value Added	%	..	..	14.2	12.5	10.5	12.0	11.8	11.7	10.7
No. of employees (thousands)		1006.1	899.5	910.5	958.0	926.9	917.1	924.3	900.7	883.5
GVA per head	£	..	..	4614	4409	4536	4367	4204	4250	4371
Implied Price Deflator[1] (1975 = 100)		60.5	60.1	66.1	82.9	100.0	119.4	146.4	168.2	187.9

All values are in 1975 prices, deflated by the Implied Price Deflator.

[1] The Implied Price Deflator is derived from Gross Output and the Index of Industrial Production (see Table 7). The Index of Industrial Production, which is based on a number of different indicators, combined with nominal output and sales figures suggest that the Wholesale Prices Index (see Table 10) understates the true extent of price inflation. The Implied Price Deflator, which reconciles these statistics, thus represents the true trend more accurately.

Net profits are equal to gross profits less depreciation.

Profit margin is the ratio of profits to total sales.

Sources: Business Monitor PA 1002: Report on the Census of Production; National Income & Expenditure Accounts.

Rising output per head has not, however, contributed to increase profitability through reducing the UK's relative unit labour costs. As already shown in Table 29, these have risen significantly for the UK relative to her main competitors. This rise contributed to the fall in profitability in 1980.

Profits have thus come under pressure from both falling demand (and hence output) and rising unit labour costs. The strengthening of sterling between 1978 and 1980 also reduced the profitability of exports.

The parts of the industry which are most vulnerable to falling profitability are low-technology machines, in which price is a most important element of demand. The price contraint means that these products can be seriously affected by rising unit labour costs or by any strengthening in sterling, which will reduce profit margins.

Falling profitability may indicate growing pressures for collaboration since firms may find it more difficult to afford projects which require a certain minimum input level. This possibility will be explored later on.[1]

5. Non-price factors in export competitiveness[2]

The import/export unit price data[3] refers to actual sales. Differences in price are thus accounted for either by a difference in the structure of the branches or because non-price factors are more important. These factors may vary from case to case, but may include :
product quality, reliability; delivery; after sales servicing and availability of spares; and so on. All these factors contribute to the customer's perception of value for money. Inability to compete on these terms may put pressure on an exporter to make a compensating reduction in price.

---

1 See pp. 170 and 177.
2 See pp. 202-205.
3 Tables 27 and 28.

A survey by the Countil of British Chambers of Commerce in Continental Europe[1] in 1979 described the main factors limiting the expansion of UK exports of non-electrical machinery into European markets as being (in order of importance):

	Market		
	W.Germany	France	Italy
1	Delivery	Delivery	Delivery
2	Suppliers' prices	Demand	Suppliers' prices
3	Image, reputation	Image, reputation	Value of sterling
4	Suppliers' support	Suppliers' prices	Suppliers' support
5	Product quality, design, etc.	Transport	Finance

According to these results, then, while the export price was consistently important it was certainly not the only factor under consideration. The National Economic Development Office (NEDO) in fact reported some years ago[2] that probably the most important single factor in strengthening the UK industry's international performance was improving delivery reliability and communication. Elsewhere, NEDO reported[3] that the ability of West German manufacturers to maintain export competitiveness in the face of a strong deutschemark in the 1970s was due to not only using productivity increases to hold prices down, but also to improving the quality, reliability and marketing of their products and generally moving up-market in the range of goods manufactured.

Thus while the UK has suffered from an uncompetitive trend in export pricing in recent years,[4] an improvement in the competitive position could be brought about through these non-price factors.

---

1 Council of British Chambers of Commerce in Continental Europe (COBCOE), 'European Survey 1979'.
2 NEDO, p.5. See also R.Rothwell.
3 D.Connell (NEDO), p.22
4 See Table 23

CHAPTER FIVE

DEVELOPMENT OF THE SURVEY

This chapter covers three sections :

i) The research methodology;
ii) The ventures;
iii) Development of the questionnaire.

The Research Methodology

The sampling frame :

In order to assess the significance of a survey on joint ventures, it was decided to compare and contrast this strategy with acquisitions. The survey therefore concentrates on these two groups. The absence of a control group is a drawback for the study; however, it is hoped that the presence of the two separate groups may overcome this deficit to a certain extent by acting as control groups upon each other.

The background research to the present study, presented in the first half of the thesis, suggested that the best way to analyse and compare international joint venture and acquisition operations would be through personal interviews; a technique not employed by most previous JV studies.[1]

Joint ventures are generally very small in comparison with their parents, and like other subsidiary companies their accounts are not published separately, but as part of the group accounts. This means that it is not possible to determine their effect on the parent group. Personal interviews mean that enormous problems of analysis and interpretation of possibly circumstantial evidence[2] can be avoided, and direct answers obtained instead. It was decided to use a structured questionnaire in order to ensure maximum comparability.

---

1 See p.46

2 For example, the occurrence of JVs in highly concentrated industries does not necessarily mean that industry concentration was a reason for the ventures.

Another notable absence from previous studies is the covering of both partners. This was considered to be an important element of the study in revealing differences of opinion regarding the objectives and success of the ventures.

An immediate problem for the study was the shortage of data on Jvs[1] and acquisitions, and on Jvs in particular. There are no lists of firms engaged in such operations, and an extensive search therefore had to be made for the purposes of the study. The constraints of funds and time inherent in a M.Phil thesis meant that the project had to be fairly limited in scope; it was initially intended to visit about 36 firms. In the event, it was possible to visit 51 companies, of which 47 are included in the study.

Given the lack of data, different methods had to be explored in order to obtain a list of British mechanical engineering firms involved in transnational JVs/acquisitions in the EEC. These fell into two main groups : (i) approaches to relevant bodies; and (ii) a search of published data.

Bodies which were approached included : 32 British and 3 European Chambers of Commerce; Six embassies and industrial development boards; the Department of Trade; the Central Office of Information; the Confederation of British Industry; the Business Co-operation Centre in Brussels; the British Institute of Management; the Industrial Credit & Finance Corporation; the Engineering Employers Federation; the Institute of Export; the Institute of Mechanical Engineers; the Engineering Industries Association, and six other engineering trade associations.

In addition , a search was carried out in newspapers, engineering journals, financial analysis publications, and company annual reports and accounts.

---

1 See p.1 for a note on the lack of statistics, and on estimates provided by the EC Commission.

Given the relevance of the project to their members' international activities, the response by the chambers of commerce was surprisingly and disappointingly weak, with only 14 of the 32 British chambers replying to requests for assistance. Eight of these published detailes of the study in their journals or newsletters, but this resulted in only one contact being established. With the exception of the Birmingham chamber, which offered a good deal of assistance,and found another participant, none of the chambers was able to give any other help in contacting firms. Generally, these bodies act as centres of trade information for their members, but have no detailed knowledge of their members' activities.

Details of the study were also published in 'Management Review and Digest' (pub. British Institute of Management); 'Export' (pub Institute of Export); and another business magazine, 'Mind Your Own Business', but again without much response.

Embassies and industrial and trade associations were also unable to give much assistance in identifying potential participants. One industrial association did suggest seven companies, but when approached these were found to either not have ventures relevant to the study, or be unwilling to participate in it. One other institute circulated its members and was able to find one company which made two contributions to the study. Since these two ventures took place some years apart in different markets, the contributions were counted as being from two separate companies. In many cases the study elicited a good deal of interest; however, many bodies were more interested in seeing the results of the survey than in helping to construct it.

The Birmingham Chamber of Industry & Commerce was able to give considerable practical help, finding one participant directly (who was in turn able to suggest another firm) and willingly making initial approaches to four large companies in its region, who had been found to have relevant ventures. In three cases, this assisted in achieving valuable contributions to the survey.

The Business Co-operation Centre (BCC) in Brussels[1] also showed

---

1 See p.13 and Appendix 1 for a review of this Centre's aims and activities.

considerable interest in the study, as it is actively involved in encouraging transnational business collaboration in the EEC. It was already known that 36 British mechanical engineering firms had approached the BCC between 1973 and 1980 in order to make contacts with firms in other EEC countries for this purpose, and a great many more had replied to requests for collaboration from companies in other Common Market states.[1] As the BCC's work ends with making initial contacts, it is not aware of the exact number of ventures which resulted, but it did agree to giving assistance in contacting the firms concerned. The BCC is forbidden by its constitution from releasing the names of firms which have used its services; however, it did co-operate by sending a copy of the research proposals to 45 British firms and asking them, if they were willing to participate in the study, to contact the Centre for European Industrial Studies directly. Contacts with six of the British participants were established in this manner.

The newspaper search revealed that a European press agency in Brussels, 'Agence Europe', publishes a daily new bulletin containing a section on 'economic interpenetration in Europe and the rest of the world', which included reports of JVs and acquisitions.[2] A search of every publication of this news sheet between mid-1974 and early 1982 was carried out at the offices of the Commission of the European Communities in London. This was by far the richest source of information, yielding details of 25 British companies involved in relevant operations - although not all of these agreed to participate.

Annual reports and accounts of public companies were considered as another source of information, but a study of a number of these did not reveal this to be a suitable source, as details of JVs were not revealed specifically in the accounts. An analysis of Extel

---

1 See Tables 5 and 6, pp.11-12.

2 The agency collects its information by having correspondents in each country. The reports thus depend on how effective the correspondents are, and can therefore lead to bias in the overall reported pattern.

company analysis cards, which can give information on 3,000 quoted companies, found that these suffered from the same weaknesses as the published reports and accounts.

As already mentioned on p.155, it was hoped to carry out interviews in about 36 companies. This would, it was assumed, necessitate contacting some 50 or 60 firms. Also, as a novelty of the study was to include interviews with EEC partners, the 36 would be split between British and EEC firms. Participating British companies would be requested to assist in making approaches to their EC partner firms.

Response rates :

The following list of JV-ing and acquiring firms was compiled:

Table 36 Sources of firms approached

Source	Jv-ing firms	Acquiring firms
Agence Europe	10	15
Chambers of Commerce	1	1
Professional Institutes	3	-
Company reports & accounts	2	-
Journal article	1	-
Personal introduction	1	1
Total	18	17

These firms were in addition to those approached by the Business Co-operation Centre. Four other firms were approached (one on the basis of its annual report & accounts; another met at a conference; the third after a suggestion by a trade association; and the fourth through a personal introduction) and interviewed, but were later excluded because their ventures were not strictly relevant (they consisted of an agency and a distribution agreement, a sales subsidiary and a non-active share participation).

A crucial problem was in deciding the best means of persuading the firms to participate in the study. In view of the relative shortage of data, it was essential that the most effective approach should be taken.

The information required by this study requires detailed knowledge of boardroom decisions on sometimes very confidential matters, and of reports on the venture from start to finish. It was therefore necessary that the questionnaires should be completed by very senior executives of the firms concerned, and an attempt was consequently made to seek participation at director level.

A postal survey was not considered to be feasible. Large firms are often approached with such questionnaires, and it would have been unrealistic to expect senior directors to devote much time to answering one. Because of this, low returns were likely to be a problem. This difficulty was magnified by the fact that the questionnaire was very long and detailed. In addition, it was felt that firms may be unwilling to commit much confidential information to a postal questionnaire. By visiting the company, the questionnaire could be worked through, questions from both sides answered immediately, and a far greater understanding of the venture achieved. Frequently, the plain answers to the printed questions were less interesting and revealing than the comments which were made during the interview.

Great emphasis was placed on convincing these companies that it would be in their own interests to participate in the study. A conviction remains that asking the firms (bearing in mind that only the most senior executives would be able to answer the questions) if they would be prepared to suffer some inconvenience in the interests of furthering the advance of knowledge would not have evoked a very effective response. Management time is very important at this level, and such executives are not normally willing to put aside an afternoon to answer an academic questionnaire. The approach to take was instead to attract the interest of these executives and offer them, for the sake of a couple of hours giving information which would remain confidential, an opportunity to learn something about an important area of business strategy.

The initial approach to the firms by letter thus mentioned the lack of previous literature in this field, and that as a consequence firms wishing to enter joint ventures in the EEC could only learn through their own experience, which could be a very costly way to learn. It then emphasised two points :

i) confidentiality would be assured, and the names of the firms would not be used in the study; also, in view of the fact that some firms would have been recognisable by the mention of their product area (where there are only a few competitors in the field), references to this would also be omitted;

ii) participating firms would receive a report on the results of the survey, so that they could see some of the practical elements involved in transnational business collaboration, and how other firms have faced the same problems.

It was also considered important to make as direct an approach as possible, by establishing the names of the managing director, finance director, marketing director and company secretary and then writing to one of them personally (usually the company secretary or managing director) and enclosing copies of the research proposals for the others, rather than addressing them more anonymously by the terms of their office.

Of course, not all the firms which were approached by this method were easily convinced. One company rejected the approach after requesting an advance copy of the questionnaire, on the grounds that : "Many of the questions relate to information which we would regard as totally confidential". In another case, a senior executive was willing to speak about a particularly sensitive (and unsuccessful) venture, but was advised against it by other members of the board and pulled out of the study. In other instances, firms replied that the executive concerned was unable to spare the time to participate.

The letters were followed up with telephone calls to help to overcome reservations.

Of the firms listed in Table 36, 13 Jv-ing and 12 acquiring firms agreed to participate,together with another 4 and 2 respectively which were obtained through the Business Co-operation Centre. The remaining

acquirer in the study had originally participated as ajoint venturer; because its two ventures had taken place in different product and geographic markets some years apart, the contributions were counted as being from separate firms.

The total number of participants in the survey were as follows:

Table 37 Survey participants, by type of firm

	Jv parent	JV subsidiaries	Acquiring firms	Acquired firms
UK firms	16	-	15	-
EEC firms	9	2	-	4

These firms covered 15 JV operations, 2 attempted JVs, 13 acquisitions and 2 attempted acquisitions. One of the JVs covered involved an interview with the European partner only. In total, then, 46 firms participated in the study.

Ideally, the study would have covered all the joint venture partners and acquired firms, but in a number of cases this was not possible. In four cases, the planned venture had not finally gone ahead; in some others the firms concerned had parted company on less than good terms; and in other instances, the UK firms felt that their partner/subsidiary[1] would be extremely suspicious of a study on the venture and did not want a contact to be made. One firm explained that its relationship was currently very delicate and wanted to avoid any questioning of its partner on potential problems, etc. Another company believed that its partner would be disturbed if it knew that the British firm had been discussing the venture. One more firm stated that its French subsidiary would believe such a study to be a subtle attempt by the parent to examine the management of the venture !

1 The term 'subsidiary' denotes an acquired subsidiary.

In other cases, however, the British firms agreed to make an initial contact with their European partner/subsidiary and request their co-operation in the study. The European firms were then approached directly. One very large German firm provided three interviews, but as these concerned different product markets, and also at different times, the contributions were counted as being from three separate companies. One of its British partners did not participate in the survey.

Although as already noted great importance was placed on seeing both partners, no attempts were made to contact either a present or former partner or subsidiary without the permission of the British company concerned, as this may have caused difficulties for the firms concerned.

All the ventures were international operations, and all involved one UK firm each (although as already stated, in one JV the UK partner did not participate). Of the JVs, three were based in Belgium, three in the Netherlands, three in France, three in West Germany, and five in the UK (of which four were with West German firms and one with an Italian firm). Of the acquisitions (all by UK firms), eleven were in France and four in West Germany. Two Dutch participants were JV subsidiaries; one being jointly owned by British and German parents, and the other by British and Dutch parents.

With very few exceptions (in which the firms concerned were in closely related sectors), the firms were involved in the mechanical engineering industries. As already noted, a precise description of the sectors concerned has been omitted in order to preserve the anonymity of the participants, who range in size from small and medium-sized firms to some of the largest engineering firms in Europe.

The earliest four ventures date from the 1960s, with twenty five of the remaining twenty eight being formed between 1976 and 1981.

The firms were seen at the following levels :

Table 38 Levels of participation, by number of firms

Managing director/chief executive	:	23
Finance Director	:	13
Sales/marketing director	:	9
Company secretary	:	3
Company chairman	:	1
Project manager	:	1
Business development executive	:	1

The number of executives interviewed exceeds that of the participants because some firms used more than one executive for the interview. One large firm,in fact, put forward its managing, finance and marketing directors.

The Ventures

The survey covered ten equity JVs (which include the creation of a new entity in which the partners take shares), five contractual JVs (which do not take a corporate form) and two attempted JVs, as well as thirteen acquisitions and two attempted acquisitions.

Although five of the JVs covered all functions from product development down to marketing, most were concerned with a single function only. Five ventures involved joint production only, and another just marketing. One venture was designed to cover both production and marketing, while another only involved co-operation between the parents on the matter of finance for the venture. The sample is not large enough for any meaningful comparison with Edstrom's results.[1]

1 See p.32.

In the case of acquisitions, however, all functions of the acquired firms are bought, and in ten cases the acquired firm continued to operate in all functional areas. Three firms were bought as pure marketing operations, however, while another two were required to continue some production but concentrate on marketing, leaving research, product development and financing to the parent.

A US study[1] found that 55% of JV parents were classified in the same broad industry group as their subsidiaries, and that 85% of the non-horizontal relationships between parents and subsidiaries involve some form of vertical integration, and a Swedish study[2] that whereas horizontal relationships are more common in acquisitions, most contractual JVs involve vertical relationships, while equity JVs are weighted towards conglomerate relationships (i.e., between manufacturing and other industries). In the present study, the distribution of relationships comes closer to that of the US study, the majority being in all three cases horizontal, as shown below :

Table 39 — Competitive relationships

Type of venture	Relationship with partner		
	Horizontal	Vertical	Conglomerate
Equity JVs	6	2	2
Contractual JVs	4	1	-
Acquisitions	12	3	-

On the question of size relationships between JVs and parents, this study does concur with previous work by Pfeffer & Nowak,[3] who found that JVs are generally very small in relation to their parents. In this study, only three of the twenty three parents indicated that the JV accounted for over 10% of their turnover. Acquisitions, on the other hand, appeared much more likely to form a significant part of their parents' activities, with seven of the fifteen acquiring firms reporting that their venture accounted for (or would have done in the case of the two attempted acquisitions) over 10% of their total sales.

1 See reference to Boyle, p.26.
2 See pp. 31-32
3 See p.40.

Two-thirds of both JVs (17/25) and acquisitions (10/15) were aimed at products which the parent also produced, but a clear distinction needs to be drawn here between this study and the US (and Edstrom's Swedish) literature,[1] which through confining themselves to the study of national operations would very likely read anti-competitive motives into such results. These, on the other hand, are international operations, and the firms concerned generally wished to use their ventures to establish themselves in a geographic market in their existing product area. Firms which do not produce the venture product sought to expand their product range into closely related areas.

In one case, the reason for the JV was to bring about a rationalisation of the existing operations of the two parents, thus enabling them to compete even more effectively against imports from a non-European multinational corporation. In almost every other case, the effect was to either introduce a new product to the market, or a new supplier of an existing product, or to increase the resources and backing available to an existing producer, thus enabling a more efficient and competitive service to result.

In no instances did an acquisition result in a reduction in the number of competitors in the market. Even though some of the ventures failed quite badly, the original intention was to provide more backing and resources to an existing competitor, thereby increasing its competitiveness in the market.

Development of the Questionnaire

The study was intended to look at the whole joint venture/ acquisition process, from conception to completion, and the questionnaire was therefore divided into six sections :

---

1 See pp. 20-42,

a) General : the parent company; its market position, relationship with the partner/victim; type of operation; market concentration and competition.

b) Motives : non-price factors in market competitiveness; previous experience; financial planning; reasons for entering the venture.

c) Search : selection of the foreign partner and market; host country investment incentives; background research.

d) Implementation : ownership, choice of the chief executive; deadlocks.

e) Operation : areas of control; transfer pricing; problem areas.

f) Success/failure : results compared with pre-stated targets; degree of success/failure; lessons learned by the firm.

a) General:

This section serves to give background information on the type of firms in the survey, the relationships involved, and competitive pressures.

Much of the US literature[1] has concentrated on the questions of whether JVs are anti-competitive, through reducing the number of effective competitors in the market, and whether firms enter them for this reason - in other words, to substitute a negotiated business environment for competitive uncertainty. Some authors[2] have proposed that the occurrence of JVs in highly concentrated industries confirms this view. An attempt was therefore made to examine the competitive structure of the industry by asking questions on market share and concentration. For reasons outlined on p.45, published concentration figures may be misleading. A subjective measure was therefore introduced, with firms giving a concentration grading of 1 to 10

---

1 See Chapter 1.

2 See, for example, pp. 21 & 24 and p. 31.

(1 being very low and 10 being monopoly). Indices constructed on the basis of market shares for the largest four or five firms would have been preferable and more comparable, but since these data are often unknown, since firms operate in different product markets, and since the fact that some of the ventures took place some years ago would have made such estimates even more difficult, this was not a viable option. 3-digit concentration ratios for the mechanical engineering industries are shown on p. 149.

A high concentration rating for the industry does not mean, however, that the strength of competition has been a reason for the venture. The evidence may be only circumstantial. A better measure of its importance (which has appeared in none of the other studies) was to ask the participants directly what role was played in their venture decision by the strength of competition in both the home and venture markets.

As with other proposed reasons, it was expected that this factor would be decisive in some venture decisions, and completely irrelevant in others.

b) Motives :

In examining motives for the venture, it is important to know what qualities are most sought after by customers. The participants were expected to believe that a corporate presence in the market would be significantly more effective than exporting to it (although exporting firms may have answered this quite differently). It would then be interesting to see whether a connection with an indigenous firm is necessitated by local nationalism,[1] and whether firm size or other factors[2] would be regarded as important issues.

---

1 The strength and importance of nationalist feelings are frequently emphasised by Mazzoline (1974), who criticises their basis of uninformed generalisations.

2 See for example, pp. 152-153.

A previous study[1] of overseas production subsidiaries found that over half the firms in the survey had invested overseas without setting financial objectives, and that firms which had carried out financial planning were more successful than those which had not. It was decided to repeat this form of question in the current survey, and also to look at the participants' attitude to risk, in order to see how much importance was attached to reducing this.

It was also decided to ask whether the participants could have produced the product concerned on the same scale by themselves, in order to identify their shortage of resources and the attractions of the local firm.

Any major differences in the strategic approach to joint ventures and acquisitions could be expected to be revealed in the reasons for entering the ventures. Both strategies involve entering the market through an established local firm and thus gaining rapid market acceptance, and both give access to the abilities of the local company.

In both cases, the key reasons from the literature for entering the venture appear to be: the speed of entry to the market (for example, through immediate access to marketing expertise or a distribution network), through which the acquiring firm also buys the existing market share of the acquired firm's own products as well as that for joint or future products; and the abilities of the local company, such as local knowledge of commercial, legal, social and political factors.

The JV-ing firm may be expected to want to (and indeed have to) rely more on its partner for participating in decisions than an acquiring firm, which may instead seek to impose centrally-determined policies on the new subsidiary, and just rely on the subsidiary to carry these out. The issue of control is likely to be important to such firms.

---

1 See p. 107.

Access to the local firm's technological ability did not feature in one study[1] of JVs by US multinational companies as being an important reason for a venture, but the structure of EEC engineering markets is such that this reason would be expected to be more important in the current study.

Another US study[2] concluded that technologically intense firms, such as in the engineering sector, enter JVs as a substitute for internal research and development expenditures. This may be confirmed by firms entering JVs in response to their partners' technological ability. Moreover, this reason would not be confined to JVs alone, but should also extend to acquisitions. Firms may buy technological ability in order to save themselves development time.

A principal difference between JVs and acquisitions is that a JV involves giving up a share of the profits in return for a reduction in the risk. JV theory would therefore suggest this to be a major reason for entering the venture. An acquisition may represent a lower risk than a greenfield venture[3] because the performance and ability of the acquired firm is (or should be, if the purchaser has done sufficient bkacground research) already known, but 'spreading the risk' is unlikely to be an important acquisition reason.

It may be difficult for firms acquiring new manufacturing subsidiaries in an overseas market to benefit from production economies of scale[4], since the distance between the plants may mean that they cannot take advantage of benefits such as joint purchasing or shared services. It is hypothesised that in international operations such as this, economies of scale are more likely to result from marketing than from production; that is, through adding to marketing capacity, firms may see increased market opportunities which they can meet from their existing manufacturing base. It is certainly possible that this can result from a JV.

---

1 See p.101
2 See pp. 36-37
3 See p. 94
4 See pp 94, 99 and 176.

A possible reason for transnational joint ventures is that because of differences in corporate taxation and company law across the EEC, and the lack of a European Company structure,[1] firms are unable to form transnational mergers, and thus co-operate instead. There is no hard evidence to support this theory, but the issue was included in the questionnaire.

Another theory is that firms enter JVs because of their own past low profitability, so that they are unable to afford to undertake ventures alone because of a shortage of capital. One project which tackled this theory[2] was unable to establish the direction of causality on whether collusion leads to low profitability or vice versa. Since JV accounts are amalgamated with those of their parents, it is impossible to say anything about their profitability, before even considering whether the JV is intended to make profits after making transfer pricing adjustments, etc. A number of criticisms can be made of this approach.[3]

This study seeks to avoid these problems by asking the participants directly what part was played in their venture decision by declining profits. It is suspected that this reason may be more commonplace than a JV study is likely to indicate, since firms seeking collaboration for this reason may not be able to find another company willing to make a capital commitment to a project with a weak partner. It is also possible that far from being a reason for collaboration, low profitability may be a reason for <u>less</u> collaboration taking place, since firms may be unlikely to be able to expand into new projects, particularly abroad, even with a partner[4].

---

1 See p.74
2 See p.39
3 See p.44
4 See p.177.

c) Search : This study also looks at the search process - examining the reasons for choosing a particular partner and country, and whether or not the firm considered alternatives. It was strongly suspected that firms which did not engage in adequate background research and planning for their venture would be less successful than those which did so. This would confirm the results of a previous study.[1]

This section will also examine the importance of regional incentives in firms' investment decisions, and whether or not these inducements had any effect on the form of venture which was adopted. One view is that investment decisions should be taken on their own merits, and government incentives only treated as a bonus if the opportunity proves to be viable, since such inducements will weaken in time, and probably reflect a deficiency of the region. Such assistance is unlikely to apply in the case of takeovers, to which firms may in fact encounter government opposition.

d) Implementation : This section looks at the ownership structure of the venture and reasons for changes. This also covers the written agreement. Another study[2] has previously suggested that potential conflicts can be overcome with a detailed agreement, and it was expected that the present study would reach similar conclusions. Also examined here is the question of deadlocks and arbitration, as well as the issue of the nationality of the chief executive. The relative advantages of using a national of the parent's country or a local national are discussed on pp. 115-116.

---

1 Newbould, Buckley & Thurwell, pp. 84-91.

2 See p.38, and also pp. 115-116.

e) Operation : Issues have been raised in the literature[1] on the question of ownership and control of the venture, and the questionnaire has therefore included a section on the degree of autonomy granted to the JV/subsidiary by the parent, and to take as an example the question of transfer pricing, by which a parent may adjut the profits of the venture in order to minimise taxation.

A question on problems encountered with the venture is included in this section. The examples offered to the firms were taken from suggestions in twelve other studies on corporate strategy, which came to the general conclusion that the problems are generally the result of two major reasons for failure: a lack of adequate pre-planning; and a lack of flexibility. If this study shows consistency with the others, the same issues can be expected to arise. The questionnaire also encouraged firms to make additional comments.

f) Success/failure : This section was designed as a summary of the venture. It therefore covers the results against pre-stated targets and the firm's assessment of their venture's success rate. It was hoped that by asking open-ended questions on lessons learned by the firm, many very useful comments could be obtained.

A great advantage of the personal interview technique is that answers to questions can be illustrated by case examples. The objective throughout the questionnaire has been to encourage firms to expand on their answers, and thus report as widely as possible their actual experiences. Bearing in mind the highly individual nature of each venture, it was hoped to avoid excessive generalisation, but it is believed that the survey is wide and deep enough to be able to find lessons which are widely applicable.

A copy of the questionnaire is in Appendix 3.

---

1 See p.113.

CHAPTER SIX

SURVEY RESULTS : MAIN ISSUES

Because of the difficulties of presenting such detailed information, it was considered best to give a general discussion on the main results of the survey in this chapter, followed by a second chapter dealing with the various sections of the questionnaire.

This chapter therefore deals with the following topics :

Reasons for entering the venture;

Results of the ventures;

Problem areas;

Lessons learned by the participants.

Reasons for entering the venture

The questionnaire listed a number of reasons for entering ventures, and the results are listed in order of importance as follows:

Table 40 Reasons for entering the venture

Rank	JV reasons	No of firms giving as most important reason	Average Score
1	Speeds of entry into the venture market[1]	8	3.50
2	Local commercial knowledge[1]	9	3.39
3	Strength of competition in venture market	8	3.04
4	Economies of scale[2]	5	3.00
5	Access to technological information or local cost benefits	4	2.77
6	Strength of competition in home market[1]	2	2.67
7	Local social and political knowledge[1]	4	2.61
8	Local legal knowledge[1]	4	2.50
9	Cost of capital	5	2.08
10	Spreading the risk	0	2.00
11	Declining profits	3	1.63
12	Assurance of source of supply[1]	0	1.00
	Transnational merger was infeasible	0	1.00

Notes : 1 Firms external to the market (i.e. not local) only.
2 Production JV parents only.

The most important reason for host companies entering JVs was assurance of source of supply (Average score: 3.13)

The number of responses exceeds the number of participants because some firms assigned equal importance to two or more factors.

Rank	Takeover reasons[1]	No of firms giving as most important reason	Average Score
1	Speed of entry into the venture market	11	4.13
2	Access to technological information or local cost benefits	3	3.20
3	Local social and political knowledge	1	3.00
4	Local legal knowledge	0	2.80
5	Local commercial knowledge	0	2.73
6	Strength of competition in venture market	2	2.40
7	Economies of scale[2]	0	1.92
8	Cost of capital	0	1.53
9	Strength of competition in home market	1	1.40
10	Spreading the risk	0	1.33
11	Assurance of source of supply	0	1.13
12	Declining profits	0	1.07
	Transnational merger was infeasible	0	1.07

Notes: 1 Acquiring firms only.
2 Excludes solely marketing ventures.

The most important reasons for acquired firms selling out were : cost of capital; spreading the risk; and declining profits (all 3.75); and assurance of source of supply (2.25).

The average score refers to a scale of importance which respondents attached to the answers (1: irrelevant; 2: not important; 3: average importance; 4: very important; 5: decisive).

In both cases, speed of entry emerged as the main reason for entering the venture,[1] although the emphasis on this factor was far greater for acquisitions than for joint ventures. Eleven of the fifteen acquiring firms stated that this was their key reason, as against eight of the eighteen external JV parents.

It is clear from the results that the JV-ing firms were much more concerned with a variety of benefits which co-operation could bring, in order to solve their own shortcomings. Thus a number of issues surfaced as being the most important one (and several in some cases) for a particular venture. Speed of entry topped the list ahead of local commercial knowledge (which more firms considered to be decisive) because it was more widely regarded as being an important factor.

---

1 The term 'venture', as distinct from 'joint venture', may be taken to refer to either type of operation.

Acquiring firms, on the other hand, were generally concerned solely with the speed of entry into the new market; victims were bought because they provided fast access to the market, and other factors were very much secondary factors.

One JV-ing firm stated : "We would rather have gone it alone than have a JV, but time was extremely important," and an acquiring firm: "We considered a greenfield venture - but it would have taken us three years."

Local commercial knowledge was rated very highly by JV-ing firms, who saw a clear distinction between this and social, political and legal knowledge, being a decisive stimulus for nine firms. For acquiring firms, this local knowledge was with one exception always a subsidiary factor, although its relatively high placing indicates that it was consistently important. But acquiring firms did not see their victims' commercial knowledge as a purchase reason in itself; indeed, its placing below the other two types of knowledge reflects the fact that such firms were more willing to rely on their own commercial knowledge than on the other types. They felt that the technological ability of the victim was a more important factor.

Three of the JV-ing firms believed that they would improve their competitive situation through eliminating competition (or the threat of it) with their JV partners.[1] One of the acquiring firms, too, was drawn by the fact that its victim[2] had been its main European rival. Other firms (one of each) were attracted by the absence of effective competition in the target market, while two JV-ing firms, and one purchaser, were forced into their venture markets by the strength of competition in their own (UK) markets.

---

1 This confirms point 4 on p.94.

2 This is standard terminology for the acquired firm. It does not indicate that the firm was unwilling to be taken over, nor that it does not receive benefits from doing so.

The hypothesis that in international operations such as this economies of scale[1] are more likely to result from marketing as opposed to production (since the operation of two production bases, geographically distant from each other, means that firms cannot take advantage of such benefits as joint purchasing or shared services), was borne out by the results. Firms looking to benefit from economies of scale appeared more likely to favour JVs than takeovers; by the former, they could see increased market opportunities which they could meet from their existing production base. Where a takeover entailed purchasing an additional manufacturing base, economies of scale were not so readily available.

Despite being widely cited in JV theory as a main reason for entering JVs,[2] not one of the 27 JV-ing firms interviewed gave 'spreading the risk' as their prime reason, and three-quarters (18/24) of the JV parents answered that this factor was of little or no importance. Although this may at first sight appear to be a most surprising result, when the question of JV size is taken into account the reason for the relative unimportance of risk becomes clear. Only three of the 23 JV parents providing such information stated that the JV accounted for over 10% of their turnover. JVs are generally very small in relation to their parents, so that the capital risk is often relatively insignificant. Firms do not generally enter JVs because they cannot afford to own the venture themselves. Still, the results do indicate that firms which were concerned with risk and the cost of capital - and also declining profits - were more likely to go for a JV than for a takeover. These factors are a recognition that the firm's own resources are insufficient, and were thus also the reasons why the acquired firms sold out.

---

1 See pp.94, 99 and 169.

2 See, for example, M.Z. Brooke & M.van Beusekom, 'International Corporate Planning', Pitman, London, 1979, p.44, and W.J.Mead 'The Competitive Significance of Joint Ventures', The Antitrust Bulletin, 1967, p.824. See also the present study, pp. 40, 100 and 169.

Both firms which tried but failed to find a suitable JV partner cited their own declining profitability[1] as a principal reason for making the attempt. As one of them put it, "we would not have considered a partner if we had still been profitable, but losses over the previous few years had caused a capital shortage." Although low profitability - so that the firm cannot afford to undertake a project on its own - may well be a reason for looking for a JV, it may also present a substantial obstacle to achieving one. Firms are generally unwilling to risk committing resources to a JV when the prospective partner is in a weak position - particularly if the partner in question is in a foreign country. But the weak firm may be acceptable to a purchaser.

It has also been suggested that firms enter transnational joint ventures and takeovers as a substitute for a true merger, made impossible by differences in fiscal and corporate laws across the EEC[2]. Not one of the firms interviewed in the study, whether engaged in JVs or in acquisitions, attached any importance whatsoever to this factor.

Apart from these reasons, several other factors were mentioned by the participants. Four firms (3 JV-ing and 1 acquiring) announced that a decisive factor had been extending their product range.

Buying a company on the basis of its availability appears to be a dangerous strategy. One of the three firms which put forward this reason saw the venture fall through before it started, but the other two both failed badly.

Three firms (2 JV-ing and 1 acquiring) decided that theirs was the cheapest way of entering the market effectively; the acquiring firm stated that the cost of this strategy was less than a third of that of a greenfield venture, and made a profit in a fraction of the time required by a greenfield. Another acquisition was made on the basis of discounted assets.[3]

---

1 See pp. 39, 44 and 170.

2 See, for example, C.Layton, 'Cross Frontier Mergers in Europe', Bath University Press, 1971. See also the European Company in Chapter 2, pp. 74-75.

3 See p. 95.

Two firms (one of each) saw their venture as a defensive strategy aimed at bolstering an existing operation, while three companies took on local manufacturing because of the importance of having a locally-made product in their markets.

Why choose one particular strategy in preference to the other? A view expressed by the managing director of one medium-sized JV-ing firm was: "Owning a small subsidiary is not the way to operate. Fixed costs form a large proportion of total costs, but the parent might not be large enough to support a larger organisation which could take advantage of economies of scale." Another firm explained its decision to enter a JV rather than adopt another strategy as follows: "We felt that after some years out of this particular product market it would be difficult to gain customer credibility and a market share if we went into production on our own. A JV gave us the ability to demonstrate to our customers our partner's commitment to our products - and of course they had a ready market share."

An acquiring firm explained that in its product area "distribution is the key factor - so we decided to acquire an established distribution network. It's easier to do that and then tell the customers that you are now in a position to sell a wider range, with more back-up, than they were buying from your distributors - especially if you can't demonstrate any significant difference in quality".

In general, the reason given for using one strategy rather than the other was simply that in the particular circumstances, it was regarded as being the most convenient means of entering the market, or of improving existing agency/distribution/licensing arrangements.

Results

The JVs and takeovers in the survey were given the following success ratings by their parent companies:

Table 41

	Venture results	
	Joint Ventures	Acquisitions
Total success	2	0
Very successful	3	3
Average success	5	5
Not successful	2	1
Failure	3	4
(Not concluded)	(2)	(2)

The JVs in this study have on average achieved a slightly better success rate than the acquisitions; however, a much larger sample would be required to form any conclusions about overall success/ failure rates for transnational JVs and takeovers in the EEC.

A closer examination of the survey results appears to indicate, however, that it is not so much the choice of strategy which contains an inherent chance of success, as much as the way in which the venture is planned. That is, joint ventures are not naturally more successful than takeovers, nor vice versa; but a carefully planned venture stands a better chance of success than an unplanned one.

This may seem to be no more than common sense - but the message needs to be emphasised if other firms are not to repeat the mistakes of some of their predecessors.

The background research undertaken by the firms was as follows, categorised by the success rates of the ventures:

Table 42 Background research classified by success rating

Success rating	Joint Ventures	Acquisitions
Total success	1. Research into product, market & partner. Long strategy development. 2. Not necessary - existing market position.	
Very successful	1. Researched market and partner. 2. Not necessary - extension of an existing arrangement. 3. Not necessary - upgrading of an existing arrangement.	1. Much desk & field work. 2. Our market knowledge + extensive fieldwork and detailed analysis of victim. 3. None.
Average success	1. Much desk & field work. 2. Product & market research. 3. Joint research with partner. 4. Not necessary - upgrading of existing agreement. 5. None.	1. Desk research, especially into victim. 2. Desk & field work. 3. Used a merchant bank to to this. 4. 3 years to research and develop the strategy, but none into the victim. 5. None - just our market knowledge.
Not successful	1. None. 2. None.	1. None - wrong decision.
Failure	1. None - bad mistake. 2. None - except into partner, which we later found was based on false information. 3. None- we're not big enough to have a research department.	1. None. 2. None. 3. None - just our market knowledge. 4. None - just our market knowledge.

These results concur with those of a previous study[1], in which 60% of the firms covered sought no market information other than what they already knew from exporting to the market in question or having an agency or sales subsidiary there.

1 G.D.Newbould, P.J.Buckley & J.C.Thurwell, 'Going International', Associated Business Press, London, 1978, pp.84-91.

It is quite clear that the firms which undertook background research were more successful on the whole than those which did not.[1] The more research is done, the better the chances of identifying possible weaknesses in the venture and either modifying it or withdrawing from it. As the managing director of one failed (and unresearched) acquisition said: "Looking back, this was a mistake. We should have done more research - it's always good to know about the market and the product, and through adding to one's knowledge one reduces the risk."

There may also be other positive spin-offs from the research. One firm claimed: "We have done lots of research into other companies around the world, filling up a huge file of about 200 firms. As a result, we came up with eight or ten really good firms. Unfortunately, since they are so good, none of them is available. But as an unintended by-product of this research we have now found that we may be able to have a JV with an Italian firm in Australia. We were not looking for this - the position has just come about through our knowledge of them in looking for a good buy. If we had not done this research, we would not have thought of a JV with them. This sort of thing just emphasises the value of research."

Problems[2]

A list of potential problems was presented to the participants, who marked them in order of importance as follows :

---

1 This again confirms Newbould, Buckley & Thurwell's results.

2 See pp. 116-117

Table 43

Problem areas

Rank	Joint Ventures	Acquisitions
1.	Marketing/distribution policy	Marketing/distribution policy
2.	Language	Language
3.	Product quality standards	Product quality standards
4.	Competition between venture and parent	Transfer pricing
5.	Transfer pricing	Production rationalisation by the parent, affecting the venture
6.	Production rationalisation by one parent, affecting the venture	Competition between venture and parent
7.	Dividend payment versus retention of earnings	Dividend payment versus retention of earnings
8.	Royalties	Royalties

Other problems mentioned include human problems, local legislation, a lack of financial and other commitment, recession conditions, and the very interesting question of the owner-manager.

The order of importance of these problems was broadly similar between the two groups, but with competition between the venture and the parent rating more highly for JVs than for acquisitions. This is only to be expected, as in the latter case the parent has full control over the venture's activities.

Marketing/distribution policy:

This was consistently the most important problem, with half of the 44 replies to this question reporting at least 'important' problems, and one-third 'very important' or 'decisive' problems in this area.

Two firms ran into problems over expansion of the operation. The managing director of one of these said: "We are already well diversified both in terms of product area and geographic markets, and are not keen on diversifying the JV any more - or at any rate, not quickly. Our partners, on the other hand, are much more restricted in their range and want to diversify much more. This could create future problems." The other firm had made an acquisition and retained the former owner-manager as chief executive, only to find that he was restricting operations to one area for his own reasons, and not for the benefit of the group.

One acquiring firm confessed to a principal reason for its failure: "We couldn't sell their products in the UK because they were too specialised for us; and since they didn't have their own sales force even in Germany - they used different agents who didn't want to know our products - there wasn't a marketing organisation which could be adapted to sell our products there." Another such firm complained: "We thought they had a good name before we bought them - but in fact they had a bad name. We couldn't negotiate any price increases because we are an English firm; and they couldn't because of their bad name." Both these companies admitted that they should have spent a lot more time on background research.

Another acquiring firm stated: "We made an unsuccessful (and costly) attempt to get (the new subsidiary) to sell a type of equipment which their existing distribution network was not capable of selling - they had no experience in that product." The firm learned that if one wants to use a subsidiary to sell a product which is additional to its range, one should check that the customers are the same - if they are in a different industry to those with which the subsidiary is accustomed to dealing, as in this case, marketing difficulties may result.

A French JV parent complained of difficulties in launching its partner's new products because its British partner was always very late with them, and the products were not available when the local firm wanted to distribute them. They complained that the British were too old fashioned, and not aggressive enough.

Finally, the manager of a Dutch JV related a problem with its UK parent. The JV had tried to sell a product (which did not compete with the parent's range, and which would otherwise not have been permitted) into a distant foreign market, and asked the local branch of the parent to help with the marketing. The local branch refused, saying that the product was out of their range. Then, when customers found out that the JV belonged to the parent, they thought something must be wrong with the product since the local firm would not deal with it. The Dutch chief executive concluded that the corporate group does not work where different product areas are involved.

Language:

Sixteen of the 44 firms replying to this question reported that language had been at least an important problem, although most firms had not been unduly troubled by it.

In one JV, three different languages were involved. The British parent spoke no German or Dutch, the German parent little English and no Dutch, and the Dutch JV spoke all three languages. At the negotiating stage it was a big problem. The personal contracts had to be translated into each language, then go through three different legal systems. Translation of technical terms was also difficult. Another British firm involved in a JV in Holland assumed that since the Dutch could speak excellent English and they could speak no Dutch, English would be used as the JV language, so they did not have this written into the agreement. As a result, they found that whenever their partners wanted to conceal something from them, they would switch into Dutch.

Several firms have encountered language problems in France, none more so than the one which admitted: "None of the French spoke English, including the Président-Directeur Général[1] (chief executive), and none of us spoke French. We sent out an English engineer but he had to come back after a couple of days - he couldn't speak French either. The PDG's inability to speak English was a significant difficulty." No attempts were made to rectify this situation, and the complete lack of communication, and the failure of the parent to integrate the French subsidiary effectively into its organisation, led to the venture's eventual collapse.

Another firm reported that although they and their French subsidiary had people who could speak each other's language, it was still a problem. A lot of this was due to cultural problems and differences rather than the actual language itself.

A number of firms believed that a local man must be in charge of the venture, and one company went as far as to say that a British manager would not be able - or allowed - to survive in France. But two purchasers had British PDGs running their French businesses

---

1 Hereafter referred to as the 'PDG'.

capably - though it should be noted that both men were perfectly fluent in French, and quite at home with the culture. One of these firms noted that language had been less of a problem since this PDG (who already worked for the parent) was appointed: "It's easier to communicate with him, not least because it gets round the problem of a culture gap between the venture and ourselves." The PDG himself added that before he took over, he had been the only person at the parent company to whom the previous PDG could talk. As the other firm's PDG said, "the seller needs to speak French - but if he doesn't also speak English he has a problem with his suppliers." Thus when the French PDG of another acquired firm took up his position, unable to speak English, and found that the British parent's capacity to speak French was well below what he had expected, he decided: "I had to learn English quickly. But when you have to speak a language, you can do so quickly. After only three weeks I could make myself understood. At first they would do translations - I would send them things in French - for accuracy." Eight years later, his English is extremely good.

Most firms did not see language as being much of a problem, although this is more likely to be due to their partner's/ subsidiary's ability to speak English than to their own ability to speak the other language. Where precision is required at board meetings, firms simply accept that board meetings last longer, while translations are being made.

Product quality standards :

Eleven firms experienced at least important problems in this area. One acquiring firm reported: "We sometimes had to replace their faulty equipment with our own (from the UK) for nothing. Their products were of rather poor quality. Even though we started selling our own parts through them, but under their name, customers would request our products, with our name - even though the actual products were the same !" The firm admitted that background research would have revealed this point beforehand.

Another firm found that there wasn't a market for its new subsidiary's products, since customers wanted machines with more uniform components. An acquired French firm complained that: "The UK companies (in the corporate group) are very jealous of their prerogative in new product development and do not allow sufficient imput from the overseas subsidiaries before developing a new product. For example, if we tell them that a particular product made in a particular way would sell well in France, they will reject it if they do not want to do it for the whole world. Then they will develop a uniform product which they want to be sold the world over - even though it might not suit are market. We get round this problem by doing some of our assembly, so that we can adapt things to the French market."

Competition between venture and parent :

This was an important problem for six JV-ing firms, against three involved in acquisitions. When a parent wishes to restrict the operations of a venture, to avoid competition with itself or other members of the corporate group, this can cause friction either with the venture itself or with the other partner. One of the participants saw another JV collapse as a direct consequence of the heated arguments with its JV partner on this issue.

Transfer pricing:

This was an important problem for three JV-ing firms and six involved in takeovers. Three of these, who had made French acquisitions, claimed that the problem did not arise directly from their own policies, but from the strengthening of sterling against the French franc since 1980, which has made British goods much less competitive in French markets. But there have also been other problems - one French firm raged that a member of its partner's corporate group was demanding to be paid in cash without even the standard 30 days credit period, "as if we were some unstable Third World Company." And the chief executive of a Dutch JV reported : "Group transfer prices are supposed to be at book value plus 4% - but this policy does not always apply in practice. One of our employees used to make (a particular piece of equipment), so he knew that they cost 50,000 NFl each. Then he was transferred to

the Middle East. He saw a market there for this product and asked (the UK parent) for two machines to start with. The price they quoted him was 400,000 NFl - hardly book value plus 4% ! Making profits out of other members of the group at intermediate stages should be eliminated, since it does not arise from extra production. We can't be sure when we do buy from the group that it is at book value plus 4% - the individual companies all look out for themselves to a certain extent."

Production rationalisation by the parent, affecting the venture :[1]

This caused problems for five firms. One managing director summed up the issue: "Production rationalisation has caused problems, with plants competing against each other to escape the axe. This causes parochialism, which would happen anyway if they were just all UK plants. It is worse across borders, though, especially when local management are convinced of their own efficiency."

One of the British chief executives running a French company gave an interesting insight into this problem: "Ceasing production was not a problem because I am a (parent company) man, had worked for them for many years, and the proposition was very reasonable and realistic. But if it had been an owner-manager PDG instead, he would have done everything he could to prevent the move. He would have put up all sorts of barriers to prevent losing the production - tried to convince the (parent) board, for example, that to sell in France the product has to be made in France, which is not true, etc."

Dividend payment versus retention of earnings:

This issue affected three firms. One, a German parent of a Dutch JV, stated that under Dutch/German double taxation it was taxed more heavily on repatriated profits than its UK partner under Dutch/UK taxation, and was therefore not as keen as the British to take out profits. The firm added, however, that this has now become less of a problem since the state of the industry is such that the profits are no longer there to take out.

---

1 See also pp 104-105.

Other problems:

Three firms complained about local legislation. One of these came up against very strict French labour laws which created difficult and very expensive problems when they tried to make redundancies as a result of closing down their manufacturing. Another firm failed in its attempt to acquire a French firm because the French authorities would not give it persmission unless it also acquired another firm, which was a most unattractive prospect. The firm was forced to pull out. By contrast, a Dutch chief executive stated: "Some of the (UK parent's) directors get very worked up about Dutch legislation - especially with regard to the workers' council. They do not seem to realise that they are wasting their time and breath raging about these things - they should just accept that it is the law."

In another case, a French firm set up a contractual JV (with consequently no capital requirements), with a UK firm. The French company then set up its own wholly-owned subsidiary to manage the operation, spending FF 6-700,000 in the process. But since it owned 100% of the new company, its British partner spent nothing. Hence while the benefits of the contractual arrangement are shared, the risks and potential losses are all down to the French. They should have gone for an equity JV.[1]

Three other firms reported problems over inadequate capitalisation of their ventures. One manager stated that his firm should also have given the JV a longer gestation period and developed a five-year plan. As he said, "you have to do it properly if you are going to do it at all."

Several other firms encountered significant human problems, ranging from a lack of willingness to get together and sort out problems with their partners, to inadequate communications resulting from personality clashes (which in one case should have been identified by sufficient prior research into the subsidiary), to a problem of 'identity'.[2] This problem arises where, following a

---

1 See p.106

2 See also pp.96, 116-117 and 196.

takeover, the new parent imposes its business systems and substantial reporting requirements on the subsidiary, removes its policy autonomy and requires it to perform for the benefit of the group as a whole rather than as an independent entity, without ensuring a programme of sympathetic integration into the group. This is likely to alienate the subsidiary employees and may well result in many of the original attractions of a takeover being lost. Motivation of the subsidiary managers is likely to be seriously affected, since they will have lost control over their own destiny. They may question their own value in an organisation which is now effectively managed by someone else, and may be unwilling to carry out dictated policies. This was certainly the reason for one failed acquisition, and occurred to a certain extent in other ventures.

The Owner-manager:

When a firm acquires an owner-managed firm, of which there are a great many in France and West Germany, it has to decide whether to retain the previous owner to manage it, or to replace him. The advantage of retaining him is that he will understand the firm better than anyone else; but there may be important disadvantages to letting him have management control. Eight firms contributed (sometimes very strong views) to the discussion.

One firm, inspired by a lack of confidence in its French distributor, bought up 51% of the equity. The firm imposed a great many reporting requirements, but allowed the old owner-manager to continue running his firm. The result was that the subsidiary's problems - based on the owner-manager's inability to distinguish between stocks and money in the bank - continued. He was also unable to understand or get to grips with reporting the sort of data which a large firm such as the parent requires. Moreover, he never kept any records, since most of his selling was done by telephone. Eventually he had to be replaced.

Another firm had similar problems with their French PDG who, although not strictly a previous owner-manager, had been with the firm for 40 years and retained old loyalties to the previous owners. Suddenly, upon acquisition, he was expected to fit into the management style of a multinational company, which demanded that every month he should send in cash flow forecasts for the next 12 months, a balance sheet, a profit & loss account - in all, a total of seventeen financial schedules, all to be at group headquarters by a set day each month. He had never done anything like this before, and could not understand the need for it - so he did not want to be bothered with it. Eventually he too had to be replaced.

In another case, a British firm initially bought 50% of a French distributor and retained the old owner-manager as PDG. This man restricted his sales to one small but highly profitable area and was unwilling to spread into other areas because this would have meant reducing his profit margin, even though in absolute terms profits would have increased. His view was that although a larger firm may bring higher absolute profits, it is also more risky. He would not comply with the British firm's instructions to expand his operations, and eventually he had to be bought out.

In other cases, firms found that they simply could not trust the owner-manager. One man had to be sacked because he was mixing the company's money up with his own. It was not a substantial amount, but he could not be trusted. Another previous owner, who carried on as the chief executive of a German company, wanted to behave in a manner which was best for him and not for the British parent. He had ensured that he retained 25.1% of the equity, so that the parent just lacked full control under German law. Significant problems followed. For example, the written agreement stated that the use of a particular subcontractor should cease "as soon as is practical." However, unknown to the British firm, the owner-manager had a financial stake in the subcontractor, and so never regarded it as practical to sever this link. After five years of such problems, the British firm managed to conclude a new management agreement by which there would now be two chief executives, and they brought in another man - also a German - from outside. This move effectively prevented the owner-manager from acting as he had done beforehand.

In another case in Germany, the British firm concerned agreed initially to form a partnership rather than an equity JV or majority shareholding, and left management control in the hands of the previous owner-manager. This man acted very much in his own interests, and concealed a good deal of information from the British firm, which as a result lost a large amount of money on the venture. The company commented on the problem: "The owner-manager is a very dangerous concept - but it would also be dangerous to buy from an owner who disappeared too quickly. What would we find there? One should perhaps keep him on for a year or two, until everything is sorted out. The difficulty with the owner-manager is that he takes things as his right, and regards your involvement as interference. Someone you bring in regards you as the boss - and rightly so. People should have to account regularly for what they are doing, rather than taking all responsibility and authority and not have to justify their actions. This is a problem of the owner-manager".

A French chief executive suggested that owner-managers should be assigned an assistant, with knowledge in every field - production, accounting and management, and that this would result in all round benefits from the owner-manager's experience and knowledge, together with improved communications and trust between the two sides. He added that the company must have people who are sufficiently open to act at a group level, not at a company level.

The managing director of one acquiring firm enthused: "The previous owner who stayed has been marvellous. It's difficult to take over a firm and then tell them how to run their own business. His performance has prevented any 'identity' clash. It is useful to have such a man, who knows the business well."

The chief executive of another French firm, on the other hand, believed that the acquiring firm should put its own man in charge from the start. He argued that an assistant would only learn what the owner-manager wanted him to learn, and that the PDG has all the power. He added, however, that the PDG must be able to speak French and know the culture - he cannot expect customers to speak his language. The problem with bringing in a manager from outside is that he would not know the subsidiary. He suggested hiring someone from another firm in the industry.

Another firm argues strongly in favour of replacing the owner-manager: "You need to be more than a firm managed by an owner-manager interested in the firm surviving as long as he survives. You need to be competitive - which means that you need money and utilisation of your profits. Whereas an owner-manager would understandably prefer to channel profits into his retirement fund and let the business bump along, you need to commit your money to the business. Also, former owners tend to be autocratic and very non-professional regarding book-keeping, auditing, etc. If you take over their firm, they can't get used to the fact that it is not their business any more. Second line managers are the same - very local to the old owner. From the new parent's point of view, there is no way you can leave it entirely to local management. You must have your people there. You must bring in outside professional management, not leave the old people in charge. How do you know they are telling you the truth otherwise ? Saying that they must do more financial reporting is not enough. What is the use in finding out about something after a decision has been taken ? Financial reporting is only historical, so you can't rely on it. The first person you need there is the financial controller, who holds the key to everything." These views were echoed by a French chief executive.

Real problems can arise where the owner-manager has aims which differ from those of the acquiring firm, and has the ability to achieve his aims and frustrate attempts by the acquirer to force a change in policy. Wherever this is possible, the firm should ensure that the owner-manager's onus of responsibility is shared, preferably by putting in an accountant with real management power.

A basic problem with the owner-manager, of course, is that if the purchaser is not willing to keep him on as chief executive, he might decide not to sell. If he is to be retained, extreme care needs to be taken over his contract.

Lessons

A number of lessons were learned by the participants, the most important of which was the need to do sufficient background research.[1] This was emphasised by no less than twelve firms, some of which had fared badly as a result of their failure to do this. As one firm said "it is extremely important to do your homework properly. Some potential partners can get uptight about this, but you should not be put off. One firm we looked into, for instance, was found to be seriously overtrading, and our money would have disappeared into a great big hole. We get a reputation for taking so long to commit ourselves - but we are sure it is the right thing to do." This research falls into different categories: the firm; the market; the product; and the country.

The firm needs to be closely examined - looking at productive capacity, product quality standards, specifications, volumes, speeds, etc. The firm's managerial competence has to be assessed, together with its reasons for selling/wanting an agreement and possible language/communication problems. One purchaser stressed that simply looking at the books is not sufficient, and that the purchaser should spend some time in the other firm before making commitment.

Market research involves spending some time talking to suppliers, customers and potential customers, finding out about attitudes to the product, faults, room for development, and the company. As one firm said, "don't commit resources without knowing that a market exists - even if the product is good."

Product analysis means examining the strengths and competitive advantages of the product with respect to other competitors, the manufacturing process, costs, and how well it fits in with existing products.

Country analysis concerns taxation and company law, labour laws, local finance, etc.

---

1 This research is described in greater detail on pp. 108-111.

The objections to research commonly concern the time and money required - but information reduces uncertainty and hence risk. One firm stated: "Sometimes you have to take a decision to make a JV or a takeover very quickly in order to exploit a market opportunity. But this doesn't mean that the decision should be any more risky than if you spent a long time on it - you should continually be updating your market knowledge and researching other companies and fields just so that you can take advantage of opportunities quickly. This continual research is very important."

It is difficult for some of the smaller firms to spare the resources required for this research; without it, however, these firms are always going to encounter problems.[1]

Six firms mentioned the importance of having a strong written agreement which is very detailed and has responsibilities and objectives clearly stated.[2] In one case, the document was really a series of agreements. It took six months to work it all out, was very complicated in parts and the partners do not refer to it in practice - but it is always there to fall back on, and there is very little room for conflict. Two other ventures had similar agreements, and in all three cases the firms agreed that their complete lack of problems was due to the extent and thoroughness of the agreement.

This does not apply only to JVs, but also to less-than-100% takeovers in which the former owner-manager remains as chief executive. One firm confessed: "We didn't even take legal advice for this agreement the first time. The owner-manager had his legal advisers and they wrote the agreement. We gave him far too much room. We only took a few weeks over it, but should have taken much longer and done it properly. It would have saved us years of problems - and in the end we have to renegotiate the agreement anyway, so it didn't save us any time at all !"

---

1 See also pp. 38 and 110.
2 See also pp. 38, 46, 115-116 and 218-219.

Another six firms believed that if one undertakes a project, one must give it enerything it needs in resources, time, commitment, etc. The venture needs to be strong in working capital, and requires a good deal of time and effort to exploit synergies. One firm summarised this group's attitude: "If one says that investment funds are not available in such amounts, or that head office is a bit thin on the ground for the necessary personnel and cannot spare them for the venture, then one should not go ahead with the operation. This also means forecasting the venture's capital requirements and capitalising it sufficiently. Do it properly or don't do it at all."

Local market knowledge and capable management are vital. For this reason, four firms stated that foreign subsidiaries should be run by local nationals. One of these believed that it is important to maintain French control for the customers' benefit, and that the customer would rather deal with other Frenchmen. But another four firms wished that they had put their own management alongside that of their new French subsidiaries. Opinions were divided on whether this should be through English-speaking Frenchmen or French-speaking Englishmen, but all four firms wanted them in the finance function, and to improve information flows to the parent. They stressed the importance of financial control.

Five firms believed that the best way of improving communication between the two sides is to create a cross-training programme - by bringing key employees from the subsidiary/partner to train with the UK firm, and vice versa. Two partners who did this extensively, even at the shop floor level, claimed that their programme had resulted in a far greater appreciation of each other's products and indeed organisations. Suggestions for areas of product development were encouraged, and achieved, at all levels within the organisations, and internal relations - and a willingness to work together - were greatly helped by the fact that individuals at all levels were personally acquainted with their counterparts. As one managing director put it, "it really doesn't cost that much, and is well worth it for the increased understanding, pride in work, elimination of alienation, etc., in which it results."

The question of identity[1] is extremely important in acquisitions, and was specifically mentioned as a lesson by four firms involved in such operations. One of them commented on its failed purchase: "We were perhaps insensitive to the subsidiary's desire for managerial autonomy, as opposed to membership of the group. We should have promoted a group identity by cross-training." The managing director of another firm, which claimed a very successful acquisition, stated: "It is difficult to change the subsidiary's mentality to that of a large company - but we have not forced the pace on them. It is important that the French feel that they are in control. Other firms have failed in the past because they have tried to force new subsidiaries to become large international firms more quickly than they could cope with the change."

The human aspect of the venture is quite crucial, and its importance cannot be over-emphasised. Problems can arise in all sorts of areas. For example, the chief executive of one company recommended: "If you take over a company whose products compete with a part of your range, do not try to sell that part of your range through them. It will lead to problems immediately. How do you propose to get a firm to sell your products in competition with their own? We did this with one company and there were problems from the very first day. The subsidiary priced our products out of the market so that they could still sell their own products. They defended this by saying that our product was more efficient, so they had to price it 15% higher, which was nothing but an excuse. The venture didn't work out at all, and we sold it back to the former owner after incurring losses." He continued: "Too many firms have had problems and run into similar losses through trying to sell their whole range through a subsidiary which has a competing product. It just won't work, and the ill-feeling and distrust which it creates can spread to other areas and affect the whole venture adversely - and the venture will fail if the people at the subsidiary are unhappy with it. If they had been more sensible and not so inflexible and greedy, they would have sold just part of their range - the complementary part - through the operation and made a success of it. Then an additional benefit would have been that the subsidiary

---

1 As discussed on pp. 96, 116-117 and 188-189.

staff would have felt that they were getting solid servicing and backing from the parent company, instead of feeling pressure and resentment."

A lesson from this study is that co-operation can work, and that problems can be overcome with care. It can and has led to other benefits, with firms doing other work for each other as a result of their venture. The level of ownership can be less important than the venture itself. As one firm, which chose a takeover because it meant 100% ownership and control rather than a smaller share in a more viable venture, commented after seeing its acquisition fail : "You don't necessarily need a majority for a good venture. A minority share in a good firm is better than a majority share in a bad one." Flexibility, co-operation and a genuine desire to work together are vital, but without proper planning this flexibility may only last until the first clash of interests arises - especially if, as one firm warned, "when you start a venture you are usually more optimistic than realistic." But backed up by sound research, a strong agreement, consideration and a real willingness to commit resources, there are many possibilities within this field.

CHAPTER SEVEN

SURVEY RESULTS, BY QUESTIONNAIRE SECTION

Continuing from the previous chapter, the present chapter gives further details of the results of the survey, by following the form of the questionnaire. The sub-sections covered are therefore those into which the questionnaire was divided, namely :

a) General;
b) Motives;
c) Search;
d) Implementation;
e) Operation; and
f) Success/failure.

a) General:

A major issue in the 'structuralist'[1] literature on JVs (as opposed to the 'strategic'[2] literature) is the question of the effect of co-operation upon competition within the industry. It has been proposed[3] that firms enter JVs in order to overcome interdependencies, and that the occurrence of JVs in highly concentrated industries confirms this view.

For reasons outlined on pp. 45 and 166-67 the participants were asked to make a subjective estimate of the strength of concentration in their home market, based on a scale of 1 to 10 (1 being very low and 10 being monopoly). The results for firms involved in both JVs and acquisitions were as follows:

---

1 i.e., regarding effects upon the structure of the industry. The same issues also apply to acquisitions.
2 i.e., concerning corporate strategy.
3 See, for example, pp. 45 and 21. For further detail on concentration in the mechanical engineering industries see pp. 145-149.

Table 44 Concentration Ratings

	Concentration Rating									
	1	2	3	4	5	6	7	8	9	10
'External' *JV parents	1	0	2	0	1	1	3	6	2	0
Host JV parents	0	1	1	0	0	0	2	1	2	0
Acquiring firms	1	1	1	1	2	5	1	2	1	0
Acquired firms	0	0	1	0	0	1	0	2	0	0

*External to the JV market.

The results show that the JV-ing firms had slightly more concentrated home markets than the acquiring firms, although the same size is not large enough to draw any conclusions from this. These figures cannot, unfortunately, give any indications as to competitive dependency because they relate to the companies' home markets. It would have been better to ask the participants to grade concentration levels in the venture market instead. Figures provided by the host country firms alone in the survey are inadequate.

However, evidence of high concentration in the external firms' home markets can give indications of 'push' factors, causing the firms to expand into other markets as a result of the strength of their domestic competition.[1] Three firms in fact reported that this factor was a decisive element in their venture decisions. As one of them stated: "Strength of competition in the UK pushed strongly towards establishing outselves in Europe, and the lower strength in France presented a competitive gap for us to exploit." and another: "Domination of the UK market by a few large firms was certainly a major factor in pushing us towards co-operation with a European firm."

1 See p. 101.

The US literature on the anticompetitive effects of JVs, which is confined to national ventures, so that both parents are within the market, does not apply in the case of transnational JVs, which are between one partner within and one partner external to the market, so that no reduction in the number of competitors can result.

Where a firm makes a JV or acquisition in another geographic market in which it does not already have a corporate presence, its experience (if any) being limited to exporting or using an agent/distributor, there are three possible effects:

i) It can result in a new product becoming available on the market, thus constituting an improvement on the previous situation. This was the effect in five of the JVs in this study.

ii) It can result in a new supplier for an existing product.[1] This, through increasing the number of domestic competitors, increases the level of domestic competition but, if it replaces previous exports of the external firm, reduced imported competition. But the increase in marketability of the external firm's products, through having the benefits of a local corporate presence, means that the first effect should exceed the second. This occurred in four of the JVs in the study.

iii) It can result in increased backing and resources for an existing producer. This again has the effect of reducing imported competition if it replaces the external firm's exports, but increases the competitiveness of the local firm. The overall effect on competition is uncertain. This was the case in seven JVs and also applied to the acquisitions.

In the remaining JV, the British firm already had a European operation. The JV resulted from a rationalisation with its major European competitor of their operations in Europe, a measure which was forced on the two firms concerned by a declining market and the need to compete effectively against imported Japanese competition. The partners have benefitted from greater operating efficiency, and although the number of competitors in the market has effectively decreased, consumer benefits have resulted from the firms' greater ability to compete against the Japanese.

---

1 See also pp.20 and 57.

A better measure of the importance of concentration and competition than examining concentration figures - which could, after all, be purely circumstantial evidence - was to ask the participants directly what part this played in their venture decisions.

Three of the JV-ing firms admitted that one reason for their ventures was that it would eliminate competition between themselves and their partners - although one firm stated that this was only a minor reason. A German firm commented: "We preferred to co-operate in the JV market rather than fight with (the partner). This JV has not, however, taken the edge off our competition with them in other areas." And a French company reported: "The key reason for this venture was the threat presented by (the partner's) potential competition with ourselves. They had a good name and a wider product range than us; they were more concerned with volume selling than with profits; and the exchange rate then was just over 9 francs to the £, which made them extremely competitive. We realised that a JV would offer us a wider range with a good name and so rather than have them compete with us we accepted their offer."

Another JV-ing firm believed that the effect of the JV would be to make it the dominant firm in Europe, and thus to achieve its objective of becoming a European market leader, while a purchaser was drawn by the fact that its target firm had been its main European rival.

On the other hand, two JV-ing firms and three acquirers reported that it was the lack of competition in the target market which was an important factor.

Thus although comments by some of the participants confirm the beliefs of some US writers to the extent that competitive interdependence in the market can be a reason for JVs, such operations can also occur when firms are drawn to a market by the opposite case, an absence of competitive interdependence, and use the ventures merely as a means of entering the market.

In many other cases, the strength or absence of competition had no impact at all on the venture decision. Such results indicate the dangers of making excessive generalisations on the reasons for business collaboration.

b) Motives :

Nearly all the firms concerned (20 out of 22 JV-ing firms replying to this question, and 18 out of the 19 involved in acquisitions) agreed that having a corporate presence in the market concerned would be significantly more effective than exporting to it. Of course, this response is only to be expected from firms which have decided to set up European operations. It is unclear how exporters would answer. A larger study using a control group could answer this question.

Almost as convincing a response was given to the question of customer nationalism.[1] 23 JV-ing firms and 15 involved in take-overs believed that local customers in the venture market were much more likely to purchase from national suppliers than from foreign firms, as opposed to 3 and 4 respectively which did not.

The firms which did not encounter local customer nationalism were united in their explanations that product quality, price, delivery, reliability and servicing[2] matter much more than the nationality of the supplying firm, although as one company admitted, a local presence makes servicing much easier. Most firms believed that qualities such as these are not in themselves sufficient to overcome the question of customer nationalism. In other words, it is not enough simply to provide such a service; the firm has in addition to be able to put a local image on the product.

---

1 See also p.43
2 See also pp. 152-153.

Firms are particularly vulnerable to this issue where the public sector is a major customer. Ten of the 23 JV-ing firms providing such information reported that over 20% of JV sales were to host country central or local government or nationalised industries. The proportion was somewhat lower for acquisition firms, with 13 out of 19 such firms reporting that less than 10% of venture sales were to public bodies.

Three firms (2 JV-ing and 1 acquiring) reported that they would have been unable to win public sector contracts without their local invovlement, and a French firm stated: "Customers would buy from any active (i.e. developing technically) and reliable company which could provide an immediate servicing capability, be it French or foreign; but there is great pressure from the government now to buy French products. For this reason, it would probably be better if we assembled our partner's products to give them a 'French-made' label." These views were echoed by another French firm, particularly regarding the pressure from the French government to buy local products in the public sector. The chief executive believed that it was very necessary to give the image of being a French company, and had therefore fought hard to prevent the UK parent from changing its subsidiary's name to match its group name.

It is possible that some people read nationalism into their failure to sell, whereas the real reason may be the firm's inability to provide an effective service without having a base in the market, or indeed their own inability to communicate with customers. As a Dutch chief executive comments: "Dutch people like German equipment - it is high quality and very new. They find UK equipment a bit old-fashioned, and are afraid of bad delivery because of strikes, etc. Nevertheless, when our German co-owner's senior man tried to sell his own products at a trade fair, he drew an absolute blank. Nobody wanted to speak to him - maybe because of historical anti-German feelings; or maybe just because he couldn't speak Dutch." Any firm which tires to sell in a market without knowing the language faces enormous difficulties.

A great many generalisations on the question of nationalism were made by the participants, along the lines of those frequently reported by Mazzolini (1974), and, because of their sweeping statements about national characters, are mostly not worth repeating. It may be because more ventures were involved in France (14) than anywhere else, but the severest criticisms were reserved for the French. A comment made by a Belgian joint venturer, and echoed by several British firms, was that: "The French are not so much nationalists as chauvinists."

Customer nationalism has not been entirely French, however, and complaints were widespread. The most extreme case was reported by a Dutch firm which had offered to supply its British parent with a particular product at two-thirds of the parent's cost of UK manufacture. The Dutch received a short reply which read simply: "We are a British company. Our customers expect us to buy British."

An interesting difference in responses between JV-ing and acquiring firms arose in the question of the importance of firm size. Whereas over half (13/24) of the JV parents believed that firm size only 5 of the 15 acquiring firms - and none of the acquired firms — is an important factor, agreed with this. Despite this, JVs were generally smaller in relation to their parents than were acquisitions, with only three of the 23 JV parents reporting that the JV accounted for over 10% of their turnover, as against seven of the 15 acquiring firms. This may reflect the fact that the greater the relative size of the venture, the greater the importance which the parent attaches to having control over it. This is quite understandable - the larger the relative size of the venture, the more it affects the nature and direction of the firm's business, over which it will quite naturally wish to retain control.

Among the firms which believed firm size to be an important factor, three reported that a successful operation requires a minimum infrastructure based on an extensive distribution network. One of these added that size gives the firm "a lot more muscle with suppliers." This point was extended by another company, which stated: "You gain more respect from customers, who know that you will have better technological ability, servicing ability, etc." Another firm

commented: "The more local people get used to seeing our equipment about, the quicker we can become established. It helps us to develop a reputation if we have a wide range." And a purchaser claimed: "Firm size is important anywhere - small firms require just as much attention as large firms, and are more difficult to turn around. Larger companies tend to beat you to contracts."

One firm encountered problems with the size of its French partner, which was too small to be able to contribute towards expanding the JV as quickly as the British firm wanted.[1] However, the larger firm was unable to buy out the operation since it would not have been able to win French public contracts without the involvement of its French partner.

Firms which replied that firm size is not important consistently argued that speed of service, reliability, quality and reputation are more important. No less than 16 firms made comments to this effect.[2] Another important issue can be continuity.[3] Customers may want to be sure that their distributors are not going to change suppliers, and also that the supplier is not going to change its distributors. The customers will wish to avoid any possible future problems over the availability of spare parts, additional products and servicing.

Nearly all the participants reported that they had some previous experience in the market concerned, listed as follows :

---

1 See p.105.
2 The importance of these non-price factors in competitiveness is described on pp. 152-153.
3 See also p.86.

Table 45 Participants' previous market experience [1]

	JV parents	Acquirers
Production subsidiary	2	0
Sales subsidiary	3	2
Licence	1	1
Distributor	1	4
Agent	8	4
None (in that product area)	2	1

One of the firms with a production subsidiary stated that the JV was based on its existing operations. The other had its production subsidiary in a different product area.

For the rest, the JV/acquisition operations represented the firms' biggest involvement yet in the market. They therefore appear to represent a stage in corporate development of a particular market, parallel to each other - since none of the firms had carried out a previous JV or acquisition in that geographic and product market.

A disturbingly high proportion (40%) of firms carried out no financial planning for the ventures.[2] This included six of the 14 equity JV-ing firms[3] and six of the 15 acquiring firms. Three of these JV-ing firms did no background research either, and it can be no surprise that two of these failed in their ventures. The other failed JV-ing firm did some financial planning, but this was unfortunately based on false information supplied by its partner. This firm also failed to carry out any background research.

Similarly, of the six acquiring firms which did no financial planning, four also did no background research. This included three of the firms which reported failures. The remaining failed acquirer did carry out some financial planning, but also failed to support this with any background research.

---

1 See Chapter 3 for descriptions of these strategies.
2 See also p.107 for a comparison with other results.
3 Firms involved in contractual JVs did no financial planning because they did not make a financial commitment and therefore carried no risk.

Where firms had failed to carry out any financial analysis, the reason given was invariably the same - that it had been a 'strategic' rather than a financial decision. However, in cases where no planning is done, and especially where no background research is carried out either, the firm may fail to identify a potentially disastrous venture, and also lacks information on the requirements of the operation. The chief executive of an acquired firm whose parent had not used any financial analysis complained: "(The parent) should have done more financial planning. They would have invested more if they had done so. (The subsidiary) was heavily under-capitalised. Our gearing was wrong for a number of years, so that we relied too much on short-term loans from banks. This proved very expensive." Fortunately, this venture was rated an 'average success'. A firm which failed badly, on the other hand, confessed: "We didn't make any financial estimates - this was a strategic decision. In short, it was a gamble which didn't pay off."

This firm, incidentally, was the only one of the seven companies which had carried out neither financial analysis nor background research which considered its investment to be a very high risk, 5 on a scale of 1 to 5 (1 = very low risk, 5 = very high risk). None of the other six rated the riskiness of their own project higher than '2'. Four of them also failed.

Business risk on such ventures can never be completely eradicated, but it can be significantly reduced by proper preparation. One purchaser (rated 'very successful) reported: "We thought the risk was fairly low because we had looked at (the acquired firm) in every conceivable way and they seemed a good, honest company. We did our own review of them, and also hired an international accountancy firm to do a business management review. They too could find nothing wrong. Basically, the risk factor came down to two points: (i) were they telling the truth (i.e., were they really a bad company in disguise) ?; and (ii) could we make them into a bad company through our own mismanagement? Even though we had investigated them as thoroughly as possible, it still had to be an intuitive decision."

Another firm, which also boasted a 'very successful' acquisition, summed up this point: "There wasn't much risk attached to the venture, since we had done sufficient research to know how (the subsidiary) would be run, and what the prospects were. In-depth research reduces uncertainty, and hence reduces risk for a viable project".

The participants were also asked, if they were unable to carry out the venture project on the same scale by themselves, what their shortage of resources was. The following factors were listed, by numbers of firms:

Table 46 Participants' shortage of Resources

	JV parents	Acquiring firms
Local management knowledge	7	0
Time	1	4
Technological ability	1	2
Larger product range	2	0
Finance	3	1
Insufficient market size	4	1
Market access & position	3	3
Distribution network	0	3

The results show some interesting differences - especially concerning local management knowledge. None of the acquiring firms indicated that their lack of this knowledge was a factor preventing them from undertaking a project alone. This is reflected in the far lower figure for acquisitions than JVs for the number of firms giving local management knowledge as a prime reason for entering the venture (see pp.173-175). Six of the above seven JV-ing firms which lacked this knowledge put it forward as a principal reason for entering their ventures. The importance of acquiring technological ability and saving development time confirm Friedman, Berg and Duncan's findings[1] that firms use knowledge-acquisition JVs as a substitute for internal R & D expenditure - although these results indicate that this reason applies very much to acquisitions as well as JVs.

---

1 See p.36.

Four other JV-ing firms believed that independent action would have been wasteful, since their output would have been constrained by market demand and not by the limits of their own resources. As one firm put it: "We could have produced the JV product on the same scale on our own, but this would have meant doing a lot of tooling up - duplicating our partner's tooling. In addition, the market would not have been large enough to support production by both firms, and so the exercise would have been wasteful. It was better to rationalise through a JV - which would also help to eliminate duplicative research and product development."

Several firms felt that they needed fast access to the market and looked for a local company with an established market position. Three acquiring firms believed that the key to success was to buy a sound, established distribution network. Having done so, all three reported successful outcomes.

c) Search :

There were two main reasons for choosing the country. Nine JV parents and eleven of the purchasing firms did so on the basis of market size and potential. On the other hand, six JV parents and four acquirers were primarily interested in the potential partner/subsidiary. In general, market size mattered where firms were interested in expanding into a new geographical market. Where they wanted to expand into a new product market or expand their current share of an existing product, the partner/subsidiary was the most important issue, and location was often largely irrelevant.

Of the firms which aimed at the partner first, two of the JV-ing ones had had previous contact with their partners as competitors. The firms were in both cases interested in developing a new product, and from their knowledge of the other firms in the industry, approached the companies which they believed could help them develop the product most effectively. In another case, a British company wanted to enter a new product market and sought to co-operate with an established European producer in order to save itself the time required to build up a reliable reputation in the product area. In a further instance, a British firm infringed the patent of another major producer in Europe, in a product area containing very few firms in the world. When the European firm challenged it on the issue, negotiations for

a licence followed, during which the firms decided that a fuller co-operation agreement would be more beneficial. Another firm, under pressure from large competitors and declining profits in its home market, attempted to find new opportunities through the Business Co-operation Centre in Brussels. This firm was just looking for opportunities rather than attempting to find a way of exploiting one. Its lack of clarity and precision in its objectives contributed greatly to its eventual failure to conclude a suitable agreement. Two other firms which used the BCC had already identified their target markets on the basis of market size, and were looking for firms in a specific area.

Of the acquiring firms which chose their subsidiaries before considering their location, one did so on the basis that its 'victim' had been its main European rival. In another case involving very few world producers, all of whom were known to each other, a British firm heard that another producer was short of finance at a time when the UK company had money to spend. The firm had made the acquisition before it realised that it should have spent more time investigating the subsidiary.

In another case, a British firm was told of a good takeover opportunity by a merchant bank, again arising from the German target firm's shortage of finance, and quickly stepped in.

The fourth firm was approached directly by the owners of an established French company, who wished to sell out. The firm realised that this would give it quick entry into the French market, in a sector marked by French nationalism in purchasing.

Of the firms which selected the market first, one German company reported that it wanted to break into the British market, but needed a British involvement to do so. There were only a few British producers, and the Germans sought a partner whose product range they could extend.

A British firm had developed a strategy to expand in Europe, but at the same time wanted to reduce its dependence on the French market, to which it was heavily committed. It selected a German partner on the basis of its availability. The venture unfortunately failed badly. Another company had already spent 2-3 years formulating a strategy of acquiring a French firm when it was approached by just such a firm. The British had actually considered and rejected this company some time before, but the French had overcome their problems in the meantime and were now considered by the UK firm to be a good buy.

Two British acquirers learned of their opportunities through personal contacts. In one case, the personal connection did not affect the takeover decision in any way, and the firm carried out a good deal of research, especially into the acquired firm, before making its commitment. The second company, which learned of its German subsidiary's availability through a personal contact, now suspects that the Germans' former owner had this information deliberately leaked to the firm, which at the time thought it was on to a bargain and snapped it up without researching it. The venture was a disaster.

A company whose experience in the French market was limited to an agent believed that it knew all the local firms in the acquired market without backing this up with research. It approached the owners of a firm which it believed had a good name but actually had a bad name and persuaded them to sell. The venture failed.

Another company which was eager to break into the French market chose its subsidiary on the basis that it was one of the only local companies not to have been taken over already by international competitors.

One more firm which had some knowledge of the French market after operating through a distributor considered that this knowledge was not sufficient. The firm employed a bilingual man solely to find it a French manufacturer of its product. It gave him a list of firms which interested it and he investigated them all, talking to the firms, other competitors, customers, etc. He drew up a short-list of four firms, of which the acquired one was the best.

The venture has been very successful.

Three firms acquired their own distributors, in one case when the firm responded to its distributor's plea for more help and products by demanding management control in return.

In another case, the British firm was principally concerned with achieving economies of scale and would only consider firms with which this could be done. Its aims have been attained, and the firm regards its venture as a total success.

One further venture came about when a European firm had grown to the point where it could no longer finance itself, and looked for buyers. A venture capital company saw an opportunity and stepped in. This company, however, has a policy of only taking minority shares in firms, in order to save itself management problems. So it asked a British firm, the largest European firm in the industry, to enter a JV with it and manage the acquisition. The British agreed, taking a majority share in the equity and managing the business.

Altogether, 16 JV-ing firms had a particular partner in mind when they considered a JV. However, only three of these firms had looked at other local companies, despite the fact that in only four ventures had a previous relationship existed between the partners. Six firms had not decided on a particular partner but were considering several; five of these firms were also considering other strategies. Seven acquiring firms also decided on their strategy with only one local company in mind, while eight others were still considering alternatives. Previous relationships existed between purchaser and subsidiary in five cases.

Most firms, whether involved in JVs or acquisitions, were attracted to partners/subsidiaries who produced complementary goods. This included 19 JV-ing firms (of which 7 were also involved in competing products) and 10 purchasers (of which 2 were also involved in competing products). Only 3 JV-ing and 3 acquiring firms formed operations with companies manufacturing competing products only.[1]

---

1 The problems of trying to sell competing products through a subsidiary are discussed on pp.196-197.

Only three companies in the whole survey felt that regional incentives were important, although nine (including seven purchasers) had looked into the question. As one firm commented: "Investment incentives are important - even if we aren't short of cash at the time. We will always look around to see what we can pick up." One company bought a 10 acre site in northern France because of regional incentives - but then found that the cost of moving production there from elsewhere in France would have been too great. Another British firm was approached by a French regional development agency as soon as the latter discovered that the former was interested in investing in France.

In not one case did these incentives have any influence at all on the form of venture adopted.

Other comments were less than favourable. One firm complained that rather than benefitting from inducements, all it had received was government hindrance in the form of, for example, taxation and competition law. Another company dismissed regional incentives as "A lot of codswallop", while the managing director of an acquiring firm stated: "The existence of regional incentives, etc, is a good enough reason for <u>not</u> investing in an area. There is bound to be a catch - lack of a transport network, suitable labour force, etc. Such incentives should be ignored for the purposes of making the investment decision (which should be based on standard business principles) and should be treated only as a bonus - <u>if</u> the investment decision is in favour of that area."[1]

The length of the decision making process for the two types of firms was as follows:

---

1 See p. 171.

Table 47 Length of the decision making process

	JV parents	Acquiring firms
0 - 2 months	3	4
3 - 5 months	2	3
6 - 11 months	7	2
12 - 18 months	8	3
over 18 months	1	2

The spread over the different time periods was fairly even for purchasers, whereas most of the JV parents took between 6 and 18 months to make their decision. The firms which took the longest, however, spent much of this time developing a market strategy rather than looking at one specific venture.

Seven firms took only a few weeks from first contact to signing the agreements. Of these, three (of which two were joint partners) failed badly, while another was graded 'not successful'. This firm should have negotiated a different type of venture, and is still having problems over this. Another company signed a poorly written agreement and suffered five years of problems before being able to renegotiate it.[1]

Four firms making French acquisitions complained that they had to wait six months for French government approval[2] before being able to carry out their operations. They were not happy about this, and one managing director stated: "This long bureaucratic delay is a big barrier to entry." In addition, acquirers are not normally permitted to purchase more than 80% of the equity of a French company, on pain of paying a tax either on the value of the subsidiary's stocks, or on the value of 'goodwill' involved in the purchase.[3] In contrast, one firm obtained French government permission quite easily and was impressed by the authorities, who allowed the firm to buy up to 95% of its subsidiary's equity without incurring the extra taxes.

---

1 See 'Lessons'. p.194.
2 See also p.96
3 See p. 112.

Another company, however, related a less fortunate experience: "The reason why this takeover did not go ahead was that the French authorities told us we could not have permission unless we also took over another company, which was a dead duck. We had even reached the stage of making representations to the French workforce. In the end we pulled out, although it's possible that the French authorities may have been bluffing."

Two firms (one of each type) reported that they also had to spend a good deal of time convincing their French associates (who were immediately very suspicious) of their good intentions. As one managing director reported: "It took many months of reassuring them that we weren't going to change the company or switch our products for their, that we didn't want to take a good French company and make it into a bad British company, that our word was good that we were going to back them up, and that we were genuine and sincere, before they would trust us."

Just under half the participants had considered alternative strategies (11 JV parents and 7 acquirers, against 13 and 8 respectively which had not). Five firms considered and rejected a greenfield venture. One of these had been unable to develop a financial model for such a strategy which gave a return within five years, "and we were unwilling to extend the pay-back period any further because uncertainty grows with time." A JV-ing firm reported: "A greenfield would have cost £7-8 million, and would have been for our own use only - there would have been little probability of selling elsewhere. We couldn't have justified it. The JV cost £3 million." One acquiring firm rejected a greenfield venture on the grounds that it would have taken three years to develop, while another such firm stated: "A greenfield would have cost £3½ million and not made a profit for the first 3-4 years. This cost us £1 million and made a profit in the first year." A joint venturer rejected the alternative of a greenfield because it did not have sufficient experienced management with the ability to speak European languages.

Among the firms which did not consider alternative strategies, one German joint venturer stated: "We would not have considered a takeover or a greenfield - both would have been too expensive. We just wanted a share of the UK market." And a British JV-ing firm reported: "If we had entered the field in (the partner's) product, we would have been 3-4 years behind them in technological ability. We wanted to get into the market quickly, so a JV suited us well." Another firm gave its reason for only considering acquisitions: "It is company policy to acquire control of all our European bases."

In other cases, two alternatives were considered. One German firm commented : "A greenfield or a takeover would have been no good at all - a waste of a lot of money. We needed a British front - and we wanted someone else to do the manufacturing. A licence or a JV - getting our products into the British market - were the ideal strategies. Which it was would have depended on our partner. If they had only wanted a licence, we would have settled for that - as long as they had good enough equipment to do the job." And a British purchaser stated: "Greenfields were not considered, since we needed an already existing distribution network. Takeovers and JVs were considered, with takeovers being considered the best choice - we would rather use the existing facilities of an established distribution system than commit other resources - bearing in mind that the French are very nationalistic in their purchasing."

Only eight of the 23 JV parents providing such information, and six of the 15 acquiring firms, had considered alternative partners/ victims. Just six firms in the survey (2 acquiring and 4 JV-ing) considered both different strategies and different partners/victims, supported by background research and financial planning, before making their commitment. Two of these ventures were rated an 'average success', three 'very successful' and one a 'total success'. This shows the value of a careful and well planned approach.

---

1 See pp. 97-98 and 102.

d) Implementation:

The question of ownership of the venture[1] is an extremely interesting area, on which a number of comments were made by the participants. One firm admitted to a certain uneasiness over the 50:50 structure of its JV: "There is no board chairman for the JV, and decisions are taken by consensus. We don't really like 50:50 ownership - we would prefer either a majority or a minority share. It is unrealistic to think that two people can run the same firm, with different ideas." Another firm in the same position made exactly the same point, and eventually gave up 0.1% of the capital, leaving itself in an overall minority position, for the sake of having a uniformity of purpose behind the running of the company.

One acquirer comments: "We like to work on the basis of full ownership or no ownership at all." But 100% ownership cannot by itself solve problems. One company which increased its shareholding in a French subsidiary from 51% to 100% because it believed that it could ensure that its policies were carried through and problems minimised with full control, found that in fact the problems became even worse after the French lost any effective rights in management decisions. As the managing director of a very successful acquirer said: "Even if you own 100%, you cannot succeed by dictating to the subsidiary. It should be their company, with our backing. The question of identity is very important."[2] A similarly successful acquirer reported: "Although we have 85% of the equity, we have not taken boardroom control, so that control of the company, being French and going hand-in-hand with the French day-to-day management, is more consistent and homogeneous. However, as majority shareholders we can always remove the board if it goes against our wishes, and appoint others instead." This firm joined with another in stressing the importance of paying regular visits to the subsidiary, and maintaining good communication and financial reporting links.

---

1 See pp. 60-61, 112-114 and p.197.
2 See pp. 116-117, 188-189 and 196.

Another company was not concerned over its lack of control over its venture. Since it manufactured the venture product, it would simply stop supplying the goods if it disagreed with the venture policy. One more firm, which owned a majority of its venture, described its associate as being very much a sleeping partner, and then added: "They wouldn't have any choice anyway - we don't take minority interests into account."

After having disagreements with their partners on the speed of expansion of their ventures, two companies expanded their equity shares, reducing their partners' exposure to the increased risk, but also their share of the venture profits.[1]

There were differences of opinion on whether the chief executive should be a local manager or a national of the parent's country.[2] It is quite clear, however, that whoever is appointed, the ability to speak the language is not enough. The chief executive needs to be able to understand colloquialisms and the way local people work and think - in other words, to understand the local culture. In addition, one firm commented on the necessity for a strong relationship between the chief executives of the JV parents: "Chief executives need to have a common understanding - objectives must be clear. They must also be flexible enough to work together without always referring back to the agreement - and on occasion to be able to do things in a different manner to the agreement. Co-operation and a desire to work together are vital. In the end, it all comes down to individual people."

The importance of having a strong written agreement is emphasised on pp. 115-116 and p. 194, and is a matter for careful consideration. As one firm stated: "Be careful in setting up the agreement - what happens if key people on your side (or the other) leave ? Don't overvalue what you bring to the table - you must be sure of what you can contribute." Of course, the agreement itself

---

1 See also p. 182.

2 See pp. 114-115 and pp. 184-185 on this issue, and also pp. 189-192 on the question of retaining former owner-managers.

will not solve everything, and the right attitude is also required. As the finance director of one UK company commented,"with the best will in the world, nothing will work if one firm wants an easy ride." The managing director of a JV-ing firm gave the following insight into this matter: "There are undertakings on what each side should do on all sorts of issues - but you can't cater for everything. A co-operative venture is like a marriage - you can't settle everything beforehand, there has to be some give and take. It is two partners working things out together. I took the written agreement out of the safe for this interview; it is the first time it has been out of the safe since it was signed, three years ago". This attitude was reaffirmed by another joint venture: "So far, neither party has even had to look at the agreement since it was signed. Both of us know that if it reaches this stage, then we do not think much of the agreement."

Where disagreements do arise, the agreement should also specify a means of solving them. As one firm confessed: "Our failure to ensure an adequate way of solving deadlocks in the original agreements has caused us no end of problems. This is a big lesson we have learned - to get the agreement right first." Where one side has control, deadlocks cannot arise. Where there is no dominant partner, or in a contractual JV, which has no capital structure, methods have to be devised of solving the issue. Two JVs had such detailed agreements that the partner could not see the question arising. Other firms had introduced 'escape' clauses into their agreements, so that the venture could simply be wound up in such an event. In three cases, the JV board members would just sit together until they could produce a mutually acceptable policy. Two ventures had agreed on arbitration in the case of disagreement - but the managing director of one of the firms involved was unhappy about this arrangement, commenting: "Arbitration has three weaknesses: it shows that the two sides cannot decide on a policy together, and that the spirit of co-operation necessary in a JV is probably not strong enough for the venture to survive; it means asking someone else to make your commercial decisions; and it can take a very long time - several months. This is a time lag that you cannot afford to wait for a decision." Arbitration is thus not an available method of solving management problems, but it can be effectively used as a last resort to prevent partners from going to court over an issue.

Finally, the finance director of a Dutch company explained a way of ending an equity JV: "The solution whereby Company A offers its JV shares to Company B at a particular price, being compelled, if Company B says the price is too high, to then buy Company B's shares at the same price, is one which we have used several times in the past. We have found that this solution works well."

e) Operation:

In seven JVs, at least one partner was a major supplier to the venture, against six ventures in which neither partner was. Five of the 13 acquiring firms providing such information were major suppliers to their subsidiaries. The following table shows trade between parents and ventures :

Table 48 — Parent - venture trade

	Percentage of venture inputs/output					
	0-10	11-20	21-40	41-60	61-80	81-100
a) Purchased from parents :						
JVs	6	0	1	1	0	5
Acquired firms	9	0	1	0	2	2
b) Sold to parents:						
JVs	11	0	0	1	0	1
Acquired firms	13	1	0	0	0	0

Very few firms were major customers of their ventures, with such trade as did occur being mainly from the parent to the venture.

Three firms sold on a 'cost plus' basis to their subsidiaries, and five parents on a normal 'arm's length' basis. Two others gave some discounts, while one company charged higher prices to its subsidiary than to outside customers, in order to keep profits in the UK. Another firm used transfer prices to minimise taxes.

In another case, one parent did the manufacturing, with the JV itself being a marketing company. Transfer prices were designed to change over time, so that to help with development costs the marketing company (i.e. the JV) would contribute towards the manufacturing costs, with the relationship reversing later on.

In another instance, the JV sells to one parent at prices well below those charged to other customers. The other partner does not mind about this arrangement, but as the purchasing parent noted, volume is low at the moment.

In an attempt to measure the autonomy of the ventures, the participants were asked which functional areas were controlled by the JV/subsidiary, and which by the parent. The results were as follows:

Table 49 Areas of control

Functional area	JV has control	JV parent retains control	Subsidiary has control	Acquiring firm retains control
Marketing	12	3	11	3
Capital expenditure	3	12	1	13
Pricing	12	3	14	0
Dividend policy	2	12	1	13
Organisation	8	7	11	3
Production planning & control	6	3	11	1

It may be seen that JVs/subsidiaries generally (though not always) have control over marketing, pricing, production planning and control (where relevant) and organisation (although for this function there is much more parental involvement in the case of JVs than for acquisitions). Parents retain control over capital expenditure (although both types of ventures are usually given discretion over expenditure up to a certain limit) and dividend policy (i.e., on profit retention and repatriation). Parent companies tend not to become involved in the day-to-day management matters, but to confine themselves to directing policy and giving authorisations on major decisions.

f) Success/failure:

The following numbers of firms achieved cost benefits from their ventures:

Table 50 — Cost benefits achieved

	JV-ing firms	Acquistion firms*
Reduction in unit costs	4	3
Savings in costs of :		
Marketing	7	2
Engineering	5	2
Administration	4	1
Reduction in R&D costs due to the elimination of duplicative research	7	2

*Includes subsidiaries.

On the whole, then, more firms involved in JVs received cost benefits than did those involved in acquisitions, although three of the latter protested that their ventures were not aimed at achieving these benefits. Benefits were not possible where the firms involved did not manufacture or sell the same products.

The results of the ventures compared with pre-stated targets (or where no planning took place, with original estimates) were as follows:

Table 51 — Venture results compared with pre-stated targets

	JVs	Acquisitions
Much greater than target	0	0
Greater than target	3	2
Met target	3	3
Fell slightly short of target	4	3
Fell considerablyshort of target	5	5

The subjective success rates of the ventures, shown on p. 179, appear to be better than the actual performance, since it was not considered to be the fault of the ventures, nor of the way in which they were handled, where the market fell off due to external economic forces. Thus some ventures which had fallen short of their pre-stated targets were still held by their parents to be successful.

In only three cases (2 JVs and 1 acquisition) were there significant differences in the way the parties concerned rated the venture.

In the case of the acquisition, the parent (which rated the venture as 'slightly short of target', and 'average success') included the early performance of the venture in its appraisal. The venture got off to a bad start, and one part of it was sold off after incurring losses. The subsidiary felt that considering the venture's inauspicious beginning, which was due to bad planning and unrealistic expectations by the parent, performance since then had been good, and the remaining part of the venture had exceeded its targetted performance. Hence it rated the result as 'greater than target', and an 'average success' overall.

In one JV, despite the fact that the market has not been very buoyant, the UK (external) firm felt that it had not fared too badly. Sales were slightly below target, but the cost of the venture to the firm was very low. Hence it rated the venture 'slightly short of target' but an 'average success'. Its partner, on the other hand, felt that the UK firm had lacked a sense of urgency in developing new products in time to match the French firm's promotion of them. Also, the French partner, through setting up its own wholly-owned subsidiary to handle what is a <u>contractual</u> JV, had spent all the money and taken all the risk involved. Sales have not been high enough to pay off its investment. It therefore rated the venture 'considerably short of target' and 'not successful'.

In the other JV, one partner was a huge European conglomerate which decided that the activity concerned did not fit in well with the rest of its group. The market had shown a considerable fall in recent years, and a good deal of rationalisation had taken place within the industry. The conglomerate decided that the high R&D costs, and the fairly low return, did not justify the retention of this activity and sold the company to its UK partner, rating the JV as 'slightly short of target' and 'not successful'. The UK firm, left the whole operation, felt that as a venture it was successful and rated it 'met target' and an 'average success'.

Taking the survey as a whole, it must be said that there have been very few instances of disagreement on answers. The participants have sometimes made criticisms of each other, and these have been mentioned under the relevant points in the results; but they have not arisen from major differences in opinion. Minor points of disagreement were, for example, over customer nationalism. Three external firms felt that this was a strong barrier, while the local firms concerned believed that other factors were more important.

On the whole, there was very little disagreement between participating partners about what had actually happened. Everybody concerned knew why ventures had gone wrong or done well. The firms were (sometimes remarkably) honest, being quite prepared to accept blame for their mistakes and to point to their own failings, without attempting to blame their partners for their own faults.

It must be admitted, however, that in only one instance did the survey cover two partners which had parted on less than amicable terms, and even in this case the firms concerned were agreed on the reasons for the collapse of their venture. In other instances it was not possible to interview one partner. Such cases can be expected to be the most likely source of disagreements and divisions between the partners.

In addition, no former owner-managers took part in the survey. Such a contribution would have been most valuable, and would have given interesting insights into the problems of the acquired firm.

A satisfying aspect of the survey was that the participants were willing to talk about their ventures whatever the outcome had been, from total success to dismal failure, and the answers given can thus be held to be a reliable guide to the practice of transnational joint ventures and acquisitions in the EEC.

Finally, eleven JV parents and seven acquiring firms announced that, as a consequence of their ventures, they were more likely to undertake another such venture in the EEC in the future. Eight and six respectively replied that the venture had made no difference to their attitudes or to the way in which they would approach future opportunties; and only four JV parents and two acquiring firms announced that they were less likely to undertake such ventures in future as a result.

Many of the participants reported that they have learned a good deal from their ventures, and that if future opportunities do arise, they will be much better equipped to handle them as a result.

APPENDIX 1

BUSINESS COOPERATION CENTRE

The aim of the Business Cooperation Centre is to encourage cooperation between firms in different Member States of the European Community, with a view to increasing their competitiveness and helping them to adjust to the expanded market.

The Business Cooperation Centre was set up by decision of the Commission of the European Communities on 21st June 1973 and is a department of the Commission, by which it is financed, but it enjoys considerable autonomy in carrying out its functions.

The staff of the Centre are under an obligation to observe confidentiality.

The Centre's services are free of charge.

DUTIES

The role of the Centre is to:

- try to find partners for firms interested in cooperation;
- provide firms with information and advice;
- keep the Community informed on obstacles of a general nature encountered by firms in their desire to cooperate or to merge.

* *

*

A. PARTNER SEARCH

1. Liaisons of the kind which it is the Business Cooperation Centre's role to encourage should be understood to mean long-term reciprocal ties which go beyond the stage of purely commercial relations.

Cooperation agreements may involve, e. g.:

- R & D (joint research, exchange of licences and know- bw);
- purchasing (joint buying of raw materials, reciprocal supplying of primary products);
- production (specialization agreements, joint production or a product, standardization of products);
- marketing and sales (joint market research, joint trademarks, reciprocal use of sales networks, joint organization of sales in a market outside the Community);
- management (joint use of management facilities).

Cooperation initiated by the Business Cooperation Centre may also take the form of financial link-ups between firms:

- setting-up of a joint subsidiary;
- acquisition of a minority holding;
- mutual acquisition of holdings;
- acquisition of a majority holding;
- setting-up of a joint holding company;
- mergers or takeovers.

On the other hand, the Business Cooperation Centre plays no part in relations of a purely commercial nature or where no mutual long-term reciprocal link is involved. Thus the following are excluded, for example:

- finding of buyers or suppliers;
- subcontracting;
- offers of or requests for commercial agencies;
- ordinary licencing agreements.

2. The Centre offers its services to all business firms of whatever legal form, financial structure or branch of activity (production, distribution, services).

The Business Cooperation Centre was created primarily to meet the needs of small- and medium-sized firms. Large undertakings will naturally have little or no reason to make use of the Centre, since they have their own economists, lawyers and tax experts who can solve the problems of international cooperation.

No strict definition of small- and medium-sized firms can be drawn up at Community level, since such a definition would of necessity vary from country to country and from sector to sector.

In a sector where activity is highly concentrated, a firm may well employ 1000 or 2000 people while nevertheless being a medium-sized firm.

The typical firm aided by the Business Cooperation Centre is one which has already made considerable use of possibilities offered by its national market and which feels ready to take advantage of the opportunities for expansion offered by the Common market.

3. The Business Cooperation Centre can deal only with cooperation between firms from the ~~nine~~ Ten member countries of the European Communities (Belgium, Federal Republic of Germany, France, Greece, Ireland, Italy, Luxembourg, Netherlands, United Kingdom). The partner firms must be of different nationalities (nationality being determined by the location of the head office).

The cooperation may, however, cover activities outside the Community (e. g., joint exports to non-member countries, establishment of a joint production subsidiary in a non-member country).

4. When a firm asks the Business Cooperation Centre to help it to find a partner with whom it can cooperate, the Centre will ask the firm to provide details about itself and to specify what type of partner and what kind of cooperation it is looking for.

The necessary additions to this written information are usually made during an interview at the firm's offices between one of the firm's directors and a member of the Centre's staff.

As soon as the Centre has a sufficiently detailed idea of the profile of the partner required and the type of cooperation or link-up wanted, the process of locating a partner is begun:

- by first of all checking whether there are suitable candidates among the offers already registered with the Business Cooperation Centre;

- by circulating an anonymous summary of the application selectively to its network of correspondents (busines associations, chambers of commerce, government bodies, banks, brokers, accountants etc.), according to the countries and sectors involved, and asking them to notify the Centre of firms which indicate their interest in the application concerned;

- if necessary by distributing this anonymous summary directly to firms which might be interested and whose names are given in directories or company lists.

When the firms reply to the Centre expressing interest in the application which has been distributed, they are usually asked to supply details about themselves corresponding to that which they have received on the applicant firm. If the firm making the reply matches the profile required, a meeting is arranged between the two potential partners.

* *

*

B. SUPPLYING INFORMATION TO FIRMS

As a rule the Business Cooperation Centre takes no part in the negotiations between firms or in the conclusion of agreements, but the Centre is always prepared to attend as a neutral third party and to provide information or advice on the opportunities for and limitations on international cooperation between firms.

The questions may deal with areas such as the following:

- company law;

- right of establishment;

- rules relating to foreign investment;

- exchange control;

- tax arrangements applying to foreign shareholders.

The questions must obviously be specific, as the Centre is not in a position to provide information covering every aspect of every type of liaison.

If the Centre receives applications which fall outside its terms of reference it will endeavour to tell the firms what persons or organizations are more competent to deal with their enquiries.

Firms may also ask the Centre for information if they have found partners by other means than through the Business Cooperation Centre.

* *
*

C. THE PROVISION OF INFORMATION TO THE COMMUNITY

Every year the Centre makes a written report to the Commission of the European Communities containing overall figures (without disclosure of the actual firms involved) showing particularly the sectors, size of firms, types of cooperation and nationalities involved and the number of successes and failures experienced; findings on the obstacles to cooperation which the firms and the Centre have encountered; and any suggestions as to what action the Community could take in this connection.

STATISTICAL EVOLUTION OF THE BUSINESS COOPERATION CENTRE (1/5/1973 - 31/12/1980)

	Year	B	D	DK	F	GB	I	IRL	L	NL	Third	TOTAL	CUM.T
INFORMATIONS	1973	43	197	33	40	190	44	14	1	28	195	785	
	1974	52	227	37	115	207	85	39	3	50	85	900	
	1975	42	64	19	101	182	78	24	2	20	42	574	2259
	1976	33	80	7	97	160	88	11	1	8	27	512	2771
	1977	26	60	5	76	193	78	12	1	16	48	515	3286
	1978	23	105	11	82	143	68	14	1	16	50	513	3799
	1979	35	42	7	92	194	74	6	2	17	106	575	4374
	1980	58	27	6	58	163	117	9	2	18	111	569	4943
OFFERS CIRCULATED	1973	4	8	-	6	18	3	-	-	-		42	
	1974	13	50	7	19	41	16	11	2	28		187	
	1975	11	12	1	20	21	21	6	-	6		98	327
	1976	3	10	1	24	19	18	2	-	-		77	404
	1977	6	8	3	21	27	10	4	-	5		84	488
	1978	3	8	3	21	20	15	4	-	5	9	88	576
	1979	13	11	3	34	29	9	2	-	4	15	120	696
	1980	8	3	1	14	21	8	4	-	3	40	102	798
REPLIES RECEIVED	1973	4	8	1	2	3	1	1	1	1		22	
	1974	247	586	39	137	209	68	55	11	74		1426	
	1975	122	292	27	162	269	57	12	3	98		1042	2490
	1976	114	236	28	111	251	58	9	2	101		910	3400
	1977	118	236	30	177	206	39	4	-	84		894	4294
	1978	92	263	29	203	262	107	23	2	83	6	1070	5364
	1979	148	361	25	399	461	168	20	5	106	44	1737	7101
	1980	247	215	9	235	269	155	11	1	104	44	1290	8391
CONTACTS ESTABLISHED	1973)												
	1974)	17	47	5	28	44	24	9	2	13		189	
	1975)												189
	1976	4	7	4	13	18	10	7	-	-		63	252
	1977	7	-	3	23	25	11	4	-	2	-	75	327
	1978	1	6	3	21	20	11	8	-	6	4	80	407
	1979	11	12	2	17	29	13	2	2	3	11	102	509
	1980	8	6	2	13	22	9	3	-	5	34	102	611

THE FIGURES FOR THIRD COUNTRIES 1980 INCLUDE THOSE FOR THE THREE CANDIDATE COUNTRIES.

APPENDIX 2

COMMISSION REGULATIONS

ARTICLE 85

1. The following practices shall be prohibited as incompatible with the Common Market: all agreements between undertakings, all decisions by associations of undertakings and all concerted practices which are liable to affect trade between Member States and which are designed to prevent, restrict or distort competition within the Common Market or which have this effect. This shall, in particular, include:

a) the direct or indirect fixing of purchase or selling prices or of any other trading conditions;
b) the limitation or control of production, markets, technical development or investment;
c) market-sharing or the sharing of sources of supply;
d) the application of unequal conditions to parties undertaking equivalent engagements in commercial transactions, thereby placing them at a competitive disadvantage;
e) making the conclusion of a contract subject to the acceptance by the other party to the contract of additional obligations which, by their nature or according to commercial practice, have no connection with the subject of such contract.

2. Any agreements or decisions prohibited pursuant to this Article shall automatically be null and void.

3. The provisions of paragraph 1 may, however, be declared inapplicable in the case of :

- any agreement or type of agreement between undertakings;
- any decision or type of decision by associations of undertakings, and
- any concerted practice or type of concerted practice

which helps to improve the production or distribution of goods

or to promote technical or economic progress, whilst allowing consumers a fair share of the resulting profit and which does not :

a) subject the concerns in question to any restrictions which are not indispensable to the achievement of the above objectives;

b) enable such concerns to eliminate competition in respect of a substantial part of the goods concerned.

ARTICLE 86

Any improper exploitation by one or more undertakings of a dominant position within the Common Market or within a substantial part of it shall be deemed to be incompatible with the Common Market and shall be prohibited, in so far as trade between Member States could be affected by it. The following practices, in particular, shall be deemed to amount to improper exploitation:

a) the direct or indirect imposition of any unfair purchase or selling prices or of any other unfair trading conditions;

b) the limitation of production, markets or technical development to the prejudice of consumers;

c) the application of unequal conditions to parties undertaking equivalent engagements in commercial transactions, thereby placing them at a commercial disadvantage;

d) making the conclusion of a contract subject to the acceptance by the other party to the contract of additional obligations which by their nature or according to commercial practice have no connection with the subject of such contract.

The regulations implementing Articles 85 and 86 are contained in Regulation No. 17 of the Council of 6.2.1962, OJ 13, 21.2.1962, p.204.

In its notice of 29.7.1968 (OJ C 75, 29.6.1968) the Commission took the view that the following agreements do not restrict competition:

1. Agreements having as their sole object:

a). An exchange of opinion or experience;

b). Joint market research;

c). The joint carrying out of comparative studies of enterprises or industries;

d). The joint preparation of statistics and calculation models.

2. Agreements having as their sole object:
a). Co-operation in accounting matters;
b). Joint provisions of credit guarantees;
c). Joint debt-collecting associations;
d). Joint business or tax consultant agencies.

These are cases of co-operation relating to fields that do not concern the supply of goods and services and the economic decisions of the enterprises involved, so that they cannot lead to restraints of competition.

3. Agreements having as their sole object:
a). The joint implementation of research and development projects;
b). The joint placing of research and development contracts;
c). The sharing out of research and development projects among participating enterprises.

It is the essence of joint research that the results should be exploited by the participating enterprises in proportion to their participation. For the assessment of the compatibility of the agreement with the rules on competition, it does not matter what legal form the common R&D takes. (In the Henkel-Colgate case, however, it was held that the prohibition of Article 85(1) can apply to joint research by two large enterprises; these two had world-wide markets and had a very strong position on the Community markets, which were characterised by their oligopolistic structure).

4. Agreements which have as their sole object the joint use of production facilities and storing and transport equipment. These forms of co-operation do not restrict competition because they are confined to organisational and technical arrangements for the use of the facilities.

5. Agreements having as their sole object the setting up of working partnerships for the common execution of orders, where the participating enterprises do not compete with each other as regards the work to be done or where each of them by itself is unable to execute the orders.

It is not a question of whether the enterprises compete with each other in other industries so much as whether in the light of the concrete circumstances of a particular case there is a possibility

in the foreseeable future they may compete with each other with regard to the products or services involved. If the absence of competition between the enterprises and the maintenance of this situation are based on concerted practices, there may be a restraint of competition.

6. Agreements having as their sole object:
a). Joint selling arrangements;
b). Joint after-sales and repair services, provided the participating enterprises are not competitors with regard to the products or services covered by the agreement.

7. Agreements having as their sole object advertising.

However, if the participating enterprises are partly or wholly prevented, by agreements or concerted practices, from themselves advertising or if they are subjected to other restrictions, there may be a restraint of competition.

8. Agreements having as their sole object the use of a common label to designate a certain quality, where the label is available to all competitors on the same conditions.

But there may be a restraint of competition if the right to use the label is linked to obligations regarding production, marketing, price formation or obligations of any other type, as is for instance the case when the participating enterprises are obliged to manufacture or sell only products of guaranteed quality.

Regulation 2821/71 of the Council, dated 20.12.1971, added the following categories to which Article 85(1), in accordance with Article 85(3), would not apply:

Agreements between undertakings, decisions of associations of undertakings and concerted practices which have as their object
a). the application of standards or types;
b). the research and development of products or processes up to the stage of industrial application, and exploitation of the results, including provisions regarding industrial property rights and confidential technical knowledge;

c). specialisation, including agreements necessary for achieving it.

Regulation 2822/71, of the same date, adds to c). : where the products which are the subject of specialisation do not, in a substantial part of the common market, represent more than 15% of the volume of business done in identical products or those considered by consumers to be similar by reason of their characteristics, price and use, and where the total annual turnover of the participating undertakings does not exceed 200 million units of account (raised to 300 million u.a. in 1977[1]).

This latter regulation is for 'block' exemptions.

The limits for agreements of minor importance, below which restrictive practices in agreements between firms would not be regarded as appreciably affecting trade between Member States or competition, are a sales level of 50 million units of account (set in 1978) or a 5% market share.[2]

1 Seventh Report on Competition Policy, point 36.
2 Ibid., points 23 and 41.

APPENDIX 3.

TRANSNATIONAL BUSINESS COLLABORATION IN THE EEC

QUESTIONNAIRE

SECTION A : GENERAL

Reference No.:

1. What was the date of the agreement? .....

2. When did it come into force? .....

3. How long was it to operate? .....

4. What nationality was your partner? .....

5. Please give your partner's name: .....

6. Please give the name of the Joint Company: .....

7. What type of operation did your firm enter? (tick)

Greenfield	
Takeover	
Share participation (state %)	
Equity JV	
Contractual JV	
Your firm taken over by another	
Another firm took a share in yours (state %)	

8. If it was a Joint Venture, what type of cooperation was involved? (tick)

Produce development	
Joint R&D	
Joint production	
Joint marketing	
Specialisation agreement	
Other (please specify)	

9. What market was the cooperation aimed at?

10. What products were involved?

11. How would you describe the relationship with your partner? (tick)

Vertical	
Horizontal	
Conglomerate	

12. What percentage of your firm's total output is accounted for by the JV? (tick)

0-10%	21-40%	61-80%	
11-20%	41.60%	61-100%	

13. Does your firm also produce the JV product? Yes/No

14. If so, what percentage of your firm's output was accounted for by this product before the JV? (tick)

0-10%	21-40%	61-80%	
11-20%	41-60%	81-100%	

15. How have your firm's exports to the JV market performed since the JV was set up, in terms of units of machinery? (tick)

Increased by 50% or more	
20-49%	
5-19%	
less than 5%	
Fallen by less than 5%	
5-19%	
20-49%	
50% or more	

16. What percentage of JV sales is to host country central or local government or nationalised industries? (tick)

0-10%	21-40%	61-80%	
11-20%	41-60%	81-100%	

17. How concentrated is your own industry?
Scale 1-10, with 1 being very low concentration and 10 being monopoly: .....

18. What is your firm's share of the domestic market? (tick)

0-10%	21-40%	61-80%	
11-20%	41-60%	81-100%	

19. What was your firm's share of the JV market (prior to the JV)? (tick)

0-10%	21-40%	61-81%	
11-20%	41-60%	81-100%	

20. How many product lines do you have? .....

21. Approximately what percentage of your sales is accounted for: (tick)

	by your main product?	by your two main products?
0-10 %		
11-20 %		
21-40 %		
41-60 %		
61-80 %		
81-100%		

22. How do imported goods in your UK market compare in terms of unit price with your own products? (tick)

Import prices higher by 20% or more	
higher by 10-19%	
higher by 5-9%	
about the same	
lower by 5-9%	
lower by 10-19%	
lower by 20% or more	

23. If there is a difference in price, does this reflect a difference in quality between UK-produced and imported products? Yes/No

24. What is the trend in UK demand for your product?

1. Did you consider that a corporate presence in the market would be significantly more effective than exporting to it? Yes/No

2. Are local customers in the JV market much more likely to purchase from national suppliers than from foreign firms? Yes/no

3. Is firm size an important factor in selling effectively to the JV market? Yes/No

4. Before setting up the JV, what experience did you have in that market? (tick)

Exporting direct		Overseas production subsidiary	
Foreign agent		Previous Joint Venture	
Distributor		Other (please specify)	
Overseas sales subsidiary			

5. What were the major tools of financial analysis used in making the investment decision?

Discounted Present Value (DPV)/ Discounted Cash Flow (DCF)	$\sum_{t=1}^{\infty} \frac{\Pi_t}{(1+r)^t}$	> I Accept < I Reject	
Net DPV (DCF)	$\sum_{t=1}^{\infty} \frac{\Pi_t}{(1+r)^t} - I$	> 0	
Internal Rate of Return	Find S such that $\sum_{t=o}^{\infty} \frac{\Pi_t}{(1+s)^t} = I$		
Pay-back period	$\sum_{t+1}^{T} \Pi_t \geq I$		
Direct profit estimates			
Other (please specify)			

6. What did you estimate on the above basis would have been the return?

6-10% loss		11-15% profit	
0-5% loss		16-20% profit	
0-5% profit		21-30% profit	
6-10% profit		over 30% profit	

7. What was the alternative strategy?

8. How would you have evaluated the riskiness of the project on a scale of 1 - 5 (1 = very low, 5 = very high)?

9. Could you have produced the JV prodcut, on the same scale as the JV, on your own? Yes/No

10. If not, could you have acquired the resources to do so? Yes/No

11. If not, what was the shortage of resources? (tick)

Finance	
Management	
Skilled labour	
Time	
Other (please specify)	

12. To what extent were the following factors important in making the JV decision? (Grade 1-5: 1 very unimportant; 2 fairly unimportant; 3 average importance; 4 fairly important; 5 very important):

Access to local cost benefits or technological information	
Local management skills including knowledge of: legal	
economic	
social and political affairs and customs	
Economies of scale	
Cost of capital make venturing alone impossible	
Spreading the risk	
Assurance of source of supply	
Speed of entry	
A merger was infeasible because of differences in tax and accounting systems	
Other (please specify)	
STRENGTH OF COMPETITION IN HOME MARKET	
STRENGTH OF COMPETITION IN JV MARKET	
DECLINING PROFITS	

SECTION C : SEARCH

1. How was the foreign partner selected?

2. Did your firm have a particular partner in mind at the time a decision to try for a JV was made? Yes/No

3. Did your firm have a previous relationship with the foreign partner - e.g. agent, distributor, licence? Yes/No

4. Does your partner produce complementary goods? Yes/No

5. Why did you choose this particular country?

6. Did you find out about host country inducements/regional incentives, and if so at what stage?

7. How important an influence were such incentives in your investment decision? (Grade 1-5 in importance, as before with 1 being very unimportant and 5 being very important) .....

8. How important an influence were such incentives in your decision to set up a JV, as opposed to other forms of market entry? (Grade 1-5, as above) .....

9. How strong is the overseas industry concerned compared with your home industry? (Grade 1-5: 1 much weaker; 2 slightly weaker; 3 about the same; 4 slightly stronger; 5 much stronger) .....

10. What methods of research were used in the search process?

11. How many months did the decision-making process take? .....

12. In that time, were alternative strategies (e.g. takeover, greenfield venture) considered? Yes/No

13. In that time, were alternative partners considered? Yes/No

SECTION D : IMPLEMENTATION

1. What was the original ownership structure of the JV?

2. How has this changed, if at all?

3. What were the reasons for any changes in the ownership structure?

4. What was the nationality of the chief executive?

5. On what basis was he chosen?

6. Did the initial agreement ensure that there was an adequate way of solving deadlocks without asking an arbitrator to make commercial decisions?

7. Did the initial agreement ensure a suitable way of terminating the venture if cooperation broke down?

SECTION E : OPERATION

1. What were the following figures, in the first year and the last (or last year, if still running) of the JV:

Pre-tax profits	
Total assets	
Sales	
Capital employed	
Exports	
Employment	

2. Is one partner a major supplier of materials or services to the JV? Yes/No
Which partner?

3. Is one partner a major customer of the JV? Yes/No
Which partner?

4. What percentage of JV inputs was purchased from the parents?

0-10%	26-50%	76-100%
11-25%	51-75%	

5. What percentage of JV output was sold to the parents?

0-10%	26-50%	76-100%
11-25%	51-75%	

6. One advantage of a JV can be to reduce the cost of a parent's inputs through the use of transfer pricing. Was there in this case a difference between transfer prices and prices to the JV's outside customers?

7. Which areas did the JV itself have control over: (tick)

Marketing	
Capital expenditure	
Pricing	
Dividend policy	
Organisation	
Production planning and control	

8. Were problems encountered over any of the following?
(Grade 1-5 in importance, with 1 being 'very unimportant' to 5 being 'very important')

Marketing/distribution policy	
Competition between the JV and one of the parents or another subsidiary	
Production rationalisation by one parent, affecting the JV	
Royalties	
Dividend payment versus retention of earnings	
Product quality standards	
Transfer pricing	
Other (please specify)	
LANGUAGE	

SECTION F : SUCCESS/FAILURE

1. Did the JV result in any of the following benefits to your firm? (tick)

Reduction in unit costs	
Savings in costs of: Marketing	
Engineering	
Administration	
Reduction in R&D costs due to the elimination of duplicative research by the parents	

2. What was your most important lesson learned from the venture?

3. What was your second most important lesson learned?

4. How did the results of the JV compare with pre-stated targets? (tick)

Much greater than target	
Greater than target	
Met target	
Fell slightly short of target	
Fell considerably short of target	

5. How would you rate the success of the JV? (tick)

Totally successful	
Very successful	
Average success	
Not successful	
Failure	

6. With the benefit of hindsight was the decision to undertake the JV correct? Yes/No

7. What, if any, factors would you now like to have changed?

8. As a result of this venture, are you more or less likely to undertake another JV in the EEC in the future?

Thank you for your help.

BIBLIOGRAPHY

Books

H.I. Ansoff, 'Corporate Strategy', Penguin, 1968.

D.G.Bean,'Financial Strategy in the Acquisition Decision', Gower, Epping, 1975.

C.Bellamy & G.Child, 'Common Market Law of Competition', Sweet & Maxwell (2nd ed.,) London, 1978.

R.L.T.Bickers, 'Marketing in Europe', Gower, London, 1971.

British Institute of Management Foundation, 'Buying a Company - A, Checklist Guide to Successful Acquisitions for the Smaller Company', B.I.M., London, 1982.

M.Z.Brooke & M. van Beusekom, 'International Corporate Planning', Pitman, London, 1979.

M.Z.Brooke & H.L.Remmers, 'The International Firm', Pitman, London, 1977.

D.F.Channon & M.Jalland, 'Multinational Strategic Planning', Macmillan, London, 1979.

D.Connell, 'The UK's performance in export markets - some evidence from international trade data', NEDO, London, 1979.

A.J.Easson, 'Tax Law and Policy in the EEC', Sweet & Maxwell, London, 1980.

European Community Investigation Services 'An ECI Business Guide to the Company Law and Related Legislation of the European Communities', London, 1980.

European Parliament Secretariat, 'Europe Today - State of European Integration 1980-81', Luxembourg, 1981.

D.Evans, 'Accountants Guide to the European Communities', Macdonald & Evans, Plymouth, 1981.

W.J. Feld, 'Transnational Business Collaboration Among Common Market Countries', Praeger, New York, 1980.

R.H.Folsom, 'Corporate Competition Law in the European Communities', Lexington Books, 1978.

L.G.Franko, 'Joint Venture Survival in Multinational Corporations', Praeger, New York, 1971.

K.D.George & C.Joll (ed), 'Competition Policy in the UK and EEC', C.U.P., 1975.

J.Hovers, 'Expansion through Acquisition', Business Books, London, 1973.

E.R.Izod, 'Growth by Merger', Industrial Mergers Ltd., London, 1968.

J.Kitching, 'Acquisitions in Europe - Causes of Corporate Successes and Failures', Business International, Geneva, 1973.

V.Korah, 'An Introductory Guide to EEC Competition Law and Practice', ESC Publishing Ltd., Oxford, 1978.

C.Layton, 'Cross Frontier Mergers in Europe', Bath University Press, 1971.

P.S.R.F. Mathijsen, 'A Guide to European Community Law', Sweet & Maxwell, London, 1972.

R.Mazzolini, 'European Transnational Concentrations', McGraw - Hill, 1974.

D.C. Mueller (ed), 'The Determinants and Effects of Mergers', Oelgeschlager, Gunn & Hain, Cambridge Mass., 1980.

G.D. Newbould, 'Management and Merger Activity', Guthstead, Doncaster, 1970.

G.D.Newbould, P.J.Buckley & J.C.Thurwell, 'Going International', Associated Business Press, London, 1978.

G.D.Newbould & G.A. Luffman, 'Successful Business Policies', Gower, Farnborough, 1978.

C.W. Oberdorfer, A.Gleiss & M.Hirsch, 'Common Market Cartel Law', 2nd ed., Commerce Clearing House Inc., Chicago, 1971.

Open University, 'Competition Policy', Open University Press, 1980.

J.C.Pollock & A.D.Jackson, 'Business Enterprises in the EEC', Institute of Chartered Accountants in England and Wales, London, 1979.

F.R. Root, 'Entry Strategies for Foreign Markets: from Domestic to International Business', Amacom, New York, 1977.

M.S.Salter & W.A.Weinhold, 'Diversification through Acquisition', The Free Press, New York, 1979.

C.Saunders, 'Engineering in Britain, West Germany and France', Sussex European Research Centre, 1978.

J.M.Stopford & L.T.Wells Jr., 'Managing the Multinational Enterprise: Organisation of the Firm and Ownership of the Subsidiaries, Longman, London, 1972.

D.Swann, 'The Economics of the Common Market,' 4th ed., Penguin, 1978.

D.Thompson, 'The Proposal for a European Company', Chatham House, London, 1969.

University of Aston in Birmingham, 'The Language Key in Export Strategy', 1981.

J.Walmsley, 'Handbook of International Joint Ventures', Graham & Trotman, London, 1982.

L.S.Walsh, 'International Marketing', 2nd ed., Macdonald & Evans, Plymouth, 1981.

M.A.Weinberg, M.V.Blank & A.L.Greystoke, 'Weinberg and Blank on Takeovers and Mergers', Sweet & Maxwell, London, 1979.

J.G.Williams, 'Acquisitions and Mergers', The Institute of Chartered Accountants in England & Wales, 1980.

G.R.Young, 'Mergers and Acquisitions - Planning and Action', Routledge and Kegan Paul, London, 1965.

Articles and other publications

P.Asch & J.J.Seneca, 'Is Collusion Profitable?', Review of Economics and Statistics, Feb. 1976, pp. 1-12.

J.Backman, 'Joint Ventures in the Light of Recent Antitrust Developments : Joint Ventures in the Chemical Industry', The Antitrust Bulletin, 1965, pp. 7-23.

E.E. von Bauer, 'Meaningful Risk and Return Criteria for Strategic Investment Decisions', Mergers and Acquisitions, Winter 1981, pp. 5-17.

J-F.Bellis, 'Potential Competition and Concentration Policy: Relevance to EEC Antitrust', Journal of World Trade Law 10(1), Jan-Feb, 1976., pp.23-49.

J.K.Bentil, 'Control of the Abuse of Monopoly Power in EEC Business Law', Common Market Law Review 12(1), Feb. 1975, pp. 59-75.

S.E.Boyle, 'An Estimate of the Number and Size Distribution of Domestic Joint Subsidiaries', Antitrust Law and Economics Review, Spring 1968, pp. 81-92.

J.Brodley, 'The Legal Status of Joint Ventures', The Antitrust Bulletin, 1976, pp. 453-483.

Business Co-operation Centre, Reports Nos. 1-8, 1974-1981.

R.E.Caves, 'International Corporations: The Industrial Economics of Foreign Investment' (1971) in J.H.Dunning (ed). 'International Investment', Penguin, 1972, pp. 265-301.

J.Chown, 'The Harmonisation of Corporation Tax in the EEC', British Tax Review, 1976, pp. 39-48.

T.P.Collier, 'Succeeding with a Joint Venture', Les Nouvelles, March 1981, pp. 27-30.

Council of British Chambers of Commerce in Continental Europe (COBCOE) 'European Survey', 1979.

J.M.Cozzolino, 'Joint Venture Risk - How to Determine Your Share', Mergers & Acquisitions, Fall 1981, pp. 35-39.

R.E.Davis, 'Compatability in corporate marriages', Harvard Business Review, July-August 1968, pp. 86 - 93.

J.H.Dunning, 'Technology, United States Investment and European Economic Growth', (1970) in J.H.Dunning (ed) 'International Investment, Penguin , 1972, pp. 377-411.

J.H.Dunning, 'The Determinants of International Production', Oxford Economic Papers, Nov. 1973, pp. 289-336.

A.J.Easson, 'Tax Harmonisation in the EEC: The Commission's Programme , British Tax Review, 1981, pp. 329-348.

A.Edstrom, 'Acquisition and Joint Venture Behaviour of Swedish Manufacturing Firms', Scandinavian Journal of Economics, 1976, pp. 477-490.

Engineering Employers Federation, 'Mechanical Engineering Short Term Trends' reports, various.

C.A.Enoch, 'Measures of competitiveness in international trade', Bank of England Quarterly Bulletin Vol. 18, No. 2, June 1978, pp. 181-195.

European Community publications: Bulletin of the European Communities - various editions. Official Journal of the European Communities - various editions. Treaty establishing the European Economic Community, Rome, 1957. European Community Review, July-August, 1972: 'Ten Years of Competition Policy.'

E.C.Commission: First (1972) to Eleventh (1982) Annual Reports on Competition Policy, Brussels/Luxembourg. Press Releases, various. 'Competition Law in the EEC and in the ECSC (situation at 30 June 1981)', Brussels/Luxembourg, 1981. 'Industrial Policy and the European Community', Luxembourg, Nov. 1972. 'Tax harmonisation in the Community', Brussels, April, 1981.

Euroforum, 10 October 1980, p.10, 'Wedding bells ring out across Europe's frontiers'.

T.Fikri, 'Review of the Evidence on Growth of Companies and Economies of Scale', in J.M.Samuels (ed) 'Readings on Mergers and Takeovers', Paul Elek Books, London, 1972, pp. 289-314.

Financial Times 27th April 1977, p.19, 'A Centre for co-operation'; 31st August 1977, p.31, 'A more aggressive role'.

G.Foster, 'The Joint Venture Gambit', Management Today, Feb. 1973, pp.75-78 and 140-144.

P.Friedman & S.V.Berg, 'Joint Ventures, Competition and Technological Complementarities : Evidence from Chemicals', Southern Economic Journal, Jan. 1977, pp. 1330-1337.

P.Friedman, S.V. Berg & J.Duncan, 'External vs internal knowledge acquisition: joint venture activity and R&D intensity', Journal of Economics and Business, Winter 1979, pp. 103-110.

W.G.Friedman, 'The Contractual Joint Venture', Columbia Journal of World Business, Jan - Feb 1972, pp. 57-63.

L.B.Gooch & R.J.Grabowski, 'Advanced Valuation Methods in Mergers and Acquisitions', Mergers & Acquisitions, Summer 1976, pp. 15-30.

S.Gullander (I), 'Joint Ventures and Corporate Strategy', Columbia Journal of World Business, Spring 1976, pp. 104-114.

S.Gullander (II), 'Joint Ventures in Europe: Determinants of Entry', in G.R.Young & J.R.Standish Bradford, 'International Studies of Management and Organisations', 1976, pp. 85-111.

C.S.P. Harding, 'Jurisdiction in EEC Competition Law : Some Recent Developments', Journal of World Trade Law 11(5), Sept-Oct 1977, pp.422-440.

M.W.Henry, 'The Competitiveness of the UK Mechanical Engineering Industry', Barclays Review, May 1981, pp. 36-39.

A.L.Herrmann, 'A Decision Model for Mergers and Acquisitions', Mergers & Acquisitions, Spring 1976, pp. 14-21.

J.D.Hlavacek, 'Towards More Successful Venture Management', Journal of Marketing, October 1974, pp 56-60.

J.V.Hlavacek & V.A. Thompson, 'The Joint Venture Approach to Technology Utilization', IEEE Transactions on Engineering Management, Feb. 1976, pp35-41.

T.Horst, 'Firm and Industry Determinants of the Decision to Invest Abroad: An Empirical Study', Review of Economics & Statistics, August 1972, pp. 258-266.

A.Jacquemin, 'Abuse of dominant position and changing European industrial structure', ch. 5 of George & Joll (ed) pp. 129-150.

R.T.Jones, 'Fundamentals of International Licensing Agreements and Their Application in the European Community', International Lawyer, 1973, pp. 78-115.

H.W. de Jong, 'EEC competition policy towards restrictive practices', ch. 2 of George & Joll (ed), pp. 33-60.

J.P.Killing (I), 'Technology Acquisition: License Agreement or Joint Venture', Columbia Journal of World Business, Fall 1980, pp. 38-46.

J.P.Killing (II), 'How to make a global joint venture work', Harvard Business Review, May-June 1982, pp. 120-127.

J.Kitching, 'Why do Mergers Miscarry?' (1967), in J.M.Samuels(ed), 'Readings on Mergers and Takeovers', Paul Elek Books, London, 1972, pp. 40-63.

H-G Koppensteiner, 'International Enterprises under the Antitrust Law of the European Economic Community', Journal of World Trade Law, 1973, pp. 287-317.

H.Levinson, 'A Psychologist Diagnosis Merger Failures' (1970), in J.M. Samuels (ed), 'Readings on Mergers and Takeovers', Paul Elek Books, London, 1972, pp. 64-76.

J.Lowe & N.Crawford, 'Technology Licensing and the Small/Medium Sized Firm', paper presented at conference, University of Bath, September, 1982.

K.Macmillan & D.Farmer, 'Redefining the boundaries of the firm', Journal of Industrial Economics, March 1979, pp. 277-285.

R.J.Mandarino, 'Joint Venture Accounting', Financial Executive, November 1977, pp. 24-31.

R.Mazzolini, 'Behavioral and Strategic obstacles to European Transnational Concentration', Columbia Journal of World Business, Summer 1973, pp. 68-78

R.Mazzolini, 'Our European mergers ? They're being ambushed by governments !', European Business, Summer 1973, pp. 26-35.

R.Mazzonlini, 'European Transnational Concentration', California Management Review, Spring 1974, pp. 43-51.

R.Mazzolini, 'European Corporate Strategies', Columbia Journal of World Business, 1975, pp. 38-49.

R.Mazzolini, 'Developing Transnational Undertakings', Journal of General Management, 1979, pp. 59-77.

W.J.Mead, 'The Competitive Significance of Joint Ventures', The Antitrust Bulletin, 1967, pp. 814-849.

M.R.Mok, 'The Jointly Owned Subsidiary ("Joint Venture") and Article 85 of the EEC Treaty', in Europa Institute of the University of Leiden (ed) 'European Competition Polucy', A.W.Sijthoff - Leiden, 1973, pp. 120-139.

D.G.Mooring, 'The Role of Licensing in the Firm', paper presented at conference, University of Bath, September 1982.

N.E.D.O. 'Marketing Study of the European Hydraulics Industry, Report No. 1: Strategy and Orgnisation', Sept. 1974.

J.Pfeffer & P.Nowak, 'Patterns of Joint Venture Activity: Implications for Antitrust Policy', the Antitrust Bulletin, 1976 pp. 315-339.

D.L.Reklau, 'Accounting for Investments in Joint Ventures - a Re-examination', Journal of Accountancy, September 1977, pp. 96-103.

L.Ritter & C.Overbury, 'An attempt at a practical approach to Joint Ventures under the EEC Rules on Competition', Common Market Law Review, 1977, pp. 601-637.

W.F.Rockwell Jr, 'How to acquire a company', Harvard Business Review, Sept-Oct. 1968, pp. 121-132.

K.J.Rosier, 'The Position Audit', International Accountant, No. 1, 1977, pp.6-8.

R.E.Ross, 'Selection of the Overseas Distributor : An Empirical Framework', International Journal of Physical Distribution, Autumn 1972, pp. 83-90.

R.Rothwell, 'Non -price factors in the export competiveness of agricultural machinery products', Research Policy Vol. 10, 1981, pp. 260-288.

S.E.Roulac, 'Structuring the Joint Venture', Mergers & Acquisitions, Spring 1980, pp. 4-14.

F.M.Scherer, 'Secrecy, the Rule of Reason, and European Merger Control Policy', The Antitrust Bulletin 19(1), Spring 1974, pp. 181-197.

D.S. Seymour, 'Your company's strengths and weaknesses - what are they ?', Chartered Mechanical Engineer, Dec. 1979, pp. 67-68.

D.S. Seymour, 'Developing a profitable business strategy - an introduction', Chartered Mechanical Engineer, Jan. 1980, pp. 67-68.

C.A. Stokes & D.R. Longmire, 'New trends in joint venture?', Hydrocarbon Processing, Nov. 1976, pp. 179-185.

J.M.Stopford & K.O. Haberich, 'Ownership and Control of Foreign Operations', Journal of General Management, Summer 1976, pp. 3-20.

J.Temple Lang, 'Joint Ventures under the EEC Treaty Rules on Competition', The Irish Jurist, 1977, pp. 15-36.

Trade and Industry, 11 June 1976, pp654-656, 'The grass isn't always greener...

D.C.Waite, 'The rise of the transnational corporation', Mckinsey Quarterly, Summer 1974, pp. 21-40.

D.C.Waite, 'The transnational corporation -corporate form for the future', European Business, Summer 1974, pp. 40-49.

J.K.Weeks, 'Licensing Agreements : Commercial and Legal Aspects', Journal of World Trade Law, 1968, pp. 285-296.

L.T.Wells, 'Joint Ventures - successful handshake or painful headache?', European Business, Summer 1973, pp. 73-79.

-----oOo-----